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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945. No. 815

PROVIDENT TRUST COMPANY OF PHILADELPHIA,
Petitioner,

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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IN THE
Supreme Court of the United States

OCTOBER TERM, 1945. No. .

Provident Trust Company of Philadelphia,
Petitioner,

v.

The Metropolitan Casualty Insurance Company of New York,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

TO THE HONORABLE, THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioner, a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, respectfully prays this Court for the issuance of a Writ of Certiorari to the Circuit Court of Appeals for the Third Circuit, to review the final judgment of that Court entered on December 17, 1945, reversing the judgment of the District Court of the United States for the Eastern District of Pennsylvania entered on July 24, 1944.

A certified transcript of the record in this case, including the proceedings in said Circuit Court of Appeals, together with the requisite additional copies thereof, is furnished herewith, in conformity with Rule 38 of this Court.

STATEMENT OF THE MATTER INVOLVED.

This case and its companion case (No. 8847 in the Circuit Court of Appeals) were tried together by the District Court and they present identical questions for decision here. The only difference is that in the companion case the plaintiff is suing as trustee and not in its individual capacity, as it does in this case.

The plaintiff is a Pennsylvania corporation and the defendant is a New York corporation. The amount involved is more than $3,000.00 and the jurisdiction of the Federal Courts is based upon the diversity of citizenship.

Judgment was for the plaintiff, now petitioner, in the District Court for the sum of $457,012.31 (R., p. 354a). This judgment was reversed by the Circuit Court of Appeals for the Third Circuit. Since neither the opinions of the District Court nor the Circuit Court have been officially reported as yet, they are attached hereto in appendix form for the convenience of this Court.

The action is against a corporate surety, Respondent, on two bonds, of the type known commonly as "completion bonds", given in connection with two building operations. To facilitate the discussion and argument hereafter the matter will be treated generally as though only one bond and one transaction were involved. This treatment is justified since the bonds differ only as to the amounts involved and the names of the builders.[1]

The District Court made findings of fact which were based upon stipulations of counsel and the testimony of

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[1] Photostatic copies of each bond and attached documents appear in the record at pages 409a and 411a.

one witness (R., pp. 48a-69a, 104a-167a, 347a, 364a). These findings are the basis of the following discussion.

The transaction giving rise to this suit was a series of building operations in 1928. The promoter of the operation, Equitable Bonded Mortgage Company (hereafter sometimes called "promoter" or "Equitable") entered into a written contract with certain builders to advance money for the operation in return for mortgages on dwellings to be erected. The first mortgages were to go to Equitable and the second mortgages to Equitable's wholly owned subsidiary, Equitable Securities Corporation (R., pp. 55a, 219a, 337a, 326a, 342a). Equitable applied to petitioner trust company for a loan to obtain a substantial part of the necessary funds, the loan to be secured by the first mortgages covering the dwellings to be erected (R., p. 140a). The petitioner made an appraisal of the proposed buildings on a completed basis, and approved the loan subject to securing a surety bond to guarantee completion (R., pp. 140a-141a, 135a).

The required bond was executed by respondent surety and builder. Equitable was named therein as obligee, but Equitable simultaneously executed a written assignment to petitioner trust company, and even prior to delivery of the bond to Equitable the respondent surety executed its formal consent to the assignment. The bond, assignment, consent to assignment, power of attorney and statement of surety's financial condition were all bound together by surety and delivered to Equitable (R., pp. 48a, 51a). On the same day Equitable delivered the document to petitioner along with the mortgages and note (R., p. 338a).

The condition of the bond was as follows:

> "NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION IS SUCH, That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above

referred to, and herein incorporated with like force and effect as if attached hereto, free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect."

The petitioner loaned Equitable a total sum of $312,000 on the two building developments; but none of the buildings was completed, and, in fact, they were hardly begun (R., pp. 50a, 106a).

The respondent surety raised several defenses in the actions on the bonds but the only one of significance here, in view of the decision of the Circuit Court of Appeals, is that based upon the fact that Equitable had breached the building agreement by failing to make the total required advances to the builder.

The District Court entered judgment for petitioner in the total amount, including interest at 3%, of $457,012.31 on July 24, 1944. Its decision was based on its finding of fact that the parties had intended that the bond should be a direct obligation from the builder and respondent surety to petitioner, and that, hence, a breach of the agreement between the builder and Equitable was immaterial.

The Circuit Court of Appeals reversed this judgment on December 17, 1945. It gave two reasons for so doing. First was its finding of fact, contrary to the District Court's, that the parties had intended only that the petitioner should take the bond by assignment, and thus the surety could raise the defense of non-performance under the builder's agreement since it could have done so in an action by Equitable, petitioner's assignor. Secondly, the Circuit Court held that under the law of Pennsylvania a bond such as this is not given for the completion of the buildings but for the performance of the building contract.

BASIS OF THIS COURT'S JURISDICTION.

This Court has jurisdiction of this case under Section 240(a) of the Judicial Code of 1911, as amended by the Act of February 13, 1925, Chap. 229, Sect. 1; 28 U. S. C. A. Sect. 347. The opinion and final judgment of the Circuit Court of Appeals were entered December 17, 1945.

QUESTIONS PRESENTED.

1. Where a surety company (respondent) executes its bond for the construction of dwellings, which bond it knew would be used as security to obtain funds for construction from a lender (petitioner), and formally consents to the assignment of that bond by the nominal obligee to the lender prior to delivery of the bond to the nominal obligee, and the District Court finds from the evidence the fact that the parties intended that the obligation should be a direct one from the surety to the lender, may the Circuit Court of Appeals overrule or disregard that finding? (Brief, *infra,* pp. 11-19).

2. Under the law of Pennsylvania is a bond conditioned on the construction of specified buildings one guaranteeing the construction of those buildings or one guaranteeing the performance of the building agreement when reference to that agreement appears only in the recital and not in the condition of the bond? (Brief, *infra,* pp. 19-27).

3. May a Circuit Court of Appeals disregard the important rule of law applied in Pennsylvania that contracts of paid sureties shall be construed strictly against them? (Brief, *infra,* pp. 27-31).

4. May a Circuit Court of Appeals apply two different standards of interpretation of written instruments in same case to the consistent benefit of a paid surety and the consistent detriment of an innocent assured? (Brief, pp. 31-33).

REASONS RELIED UPON FOR GRANTING THE WRIT.

The discretionary power of this Court to grant a Writ of Certiorari is invoked upon the following grounds:

1. The Circuit Court of Appeals for the Third Circuit has departed so far from the accepted and usual course of judicial procedure, based upon Rule 52(a) of the Federal Rules of Civil Procedure and decisions of this Court, in overruling a District Court's finding of fact as to which there is substantial evidence, that this Court should exercise its supervisory powers.

2. The Circuit Court of Appeals for the Third Circuit has decided important questions of Pennsylvania law as to the proper interpretation of surety bonds in conflict with applicable Pennsylvania decisions.

3. The Circuit Court of Appeals for the Third Circuit has departed so far from the accepted and usual course of judicial proceedings by applying inconsistently two different standards of interpretation to the contracts involved in this case that this Court should exercise its supervisory powers.

WHEREFORE, your petitioner respectfully prays that a Writ of Certiorari be issued under the Seal of this Court, directed to the United States Circuit Court of Appeals for the Third Circuit, commanding said Court to certify and send to this Court on a day to be designated, a full and complete transcript of the record and all proceedings

of said Circuit Court of Appeals had in this cause, to the end that this cause may be reviewed and determined by this Court; that the judgment of said Circuit Court of Appeals be reversed; and that your petitioner be granted such other and further relief as to this Honorable Court may seem meet.

PROVIDENT TRUST COMPANY OF PHILADELPHIA,

By

WM. CLARKE MASON,

Counsel for Petitioner.

PHILADELPHIA,
February 5, 1946.

BRIEF APPLICABLE TO THIS AND COMPANION CASE IN SUPPORT OF BOTH PETITIONS.

I. OPINIONS OF THE COURTS BELOW.

The opinions of the District Court appear in the Record at pages 337a, 349a and 362a. They have not yet been officially reported. The opinion of the Circuit Court of Appeals, a part of the Record, has not yet been officially reported.

The opinions of both Courts are attached hereto in appendix form for the convenience of this Court.

II. JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code of 1911, as amended by the Act of February 13, 1925, Chap. 229, Sect. 1, 43 Stat. 936, 28 U. S. C. A., Sect. 347.

The judgment of the United States Circuit Court of Appeals for the Third Circuit, which Petitioner seeks to have reviewed, was filed on December 17, 1945.

III. STATEMENT OF THE CASE.

The essential facts on which this application rests are stated in the foregoing Petition for Writ of Certiorari. Insofar as may be required for a clear understanding of the several points of the ensuing argument, these facts will be supplemented by further references to the Record.

IV. SPECIFICATIONS OF ERROR.

The error which Petitioner intends to urge, if the Writ of Certiorari is granted, is that the Circuit Court of Appeals erred:

In failing to follow the finding of fact made by the District Court that the parties intended that the bond should run directly to Petitioner to secure its loans.

In holding, contrary to applicable decisions of the Supreme Court of Pennsylvania, that a bond given to secure the completion of buildings is conditioned upon the performance of the building agreement and not the construction of the buildings, even though the building agreement is referred to only in a recital.

In failing to follow the Pennsylvania rule that contracts of paid sureties will be construed strictly against them.

In failing to apply a consistent rule of interpretation as to the several agreements involved.

V. SUMMARY OF ARGUMENT.

1. The Circuit Court of Appeals disregarded the District Court's findings of fact which were supported by substantial evidence.

2. The construction placed upon the conditions of the bonds by the Circuit Court of Appeals is in conflict with applicable Pennsylvania decisions.

3. The rule, sustained by Pennsylvania decisions and decisions of this Court, that the contracts of paid sureties are to be construed strictly against them has not been followed by the Circuit Court of Appeals in these cases.

4. The decision of the Circuit Court of Appeals contains such a fundamental inconsistency that it constitutes a serious departure from the usual course of judicial procedure.

The Circuit Court of Appeals Disregarded the District Court's Findings of Fact Which Were Supported by Substantial Evidence.

The District Court adopted the stipulation of facts as part of its special findings of fact, and stated that "The statements of fact in the opinion may be taken as additional special findings, supplementing or modifying the facts as stipulated, and answering such requests as are not covered by the stipulation" (Appendix, p. 11a).

The District Court found as a fact from the circumstances involved that it was the intention of the parties that the bond was to run directly to the petitioner to secure its loan despite the fact that the transaction was in the form of a simultaneous assignment of the bond.

In its opinion, sur motion for new trial, the District Court summarized its original findings by making the following statement (Appendix, p. 12a).

> "In reaching its conclusions the court examined the entire transaction and *found that the bond was intended to run directly to the plaintiff to secure its loan,* the plaintiff being the real obligee, that the building operation had been undertaken by, or through the medium of, Equitable Bonded Mortgage Company and that Equitable, although on paper an obligee, was in reality and to the knowledge of the plaintiff in the position of a principal along with the building contractor (the nominal principal)." (Emphasis supplied.)

Under Rule 52(a) of the Federal Rules of Civil Procedure, it is stated that findings of fact shall not be set aside unless clearly erroneous.

Despite this clear injunction as to the effect to be given to findings of fact made by the trial court, the Circuit Court of Appeals for the Third Circuit saw fit to overrule the aforesaid finding of fact by the District Court

that the parties intended the petitioner to be a direct obligee. The Circuit Court of Appeals said (Appendix, p. 20a): "We do not see that the various facts urged by the Plaintiff to show that Provident was a direct obligee, prove the conclusion." At the time the Court made this statement the conclusion was an express finding of fact by the District Court and was no longer merely Petitioner's conclusion.

That there is ample evidence to support the District Court's finding as to the intention of the parties is apparent from the following evidentiary facts also found by the District Court and affirmed by the Circuit Court of Appeals (Appendix, pp. 18a-19a):

(1) The Respondent surety knew that the Petitioner and not the Equitable Bonded Mortgage Company was to be the ultimate recipient of the bonds.

(2) The assignment and consent to assignment, by Respondent surety, were executed before the bonds were even delivered to the nominal obligee, Equitable Bonded Mortgage Company, by Respondent surety.

(3) In each case the bond, assignment, consent to assignment, power of attorney authorizing the execution of the bond and a statement of Respondent's financial condition, were bound together as one instrument by Respondent surety prior to delivery to the nominal obligee, Equitable Bonded Mortgage Company.

(4) The whole transaction of delivery by Respondent surety to Equitable Bonded Mortgage Company and then to Petitioner was completed on the same day so that Equitable held the bonds only momentarily.

(5) The Petitioner required that construction bonds be furnished as collateral before it would loan its money to Equitable Bonded Mortgage Company.

In the light of these basic facts it is impossible to say that the ultimate finding of the District Court was "clearly erroneous"; and it is only on such a basis that the Circuit Court of Appeals had the power to disregard it.

Prior to the adoption of Rule 52 (a) this Court had already held that an appellate court cannot review the evidence for the purpose of drawing its own inference or conclusion therefrom at variance with the trial judge's finding of fact. Thus, in *McCaughn* v. *Real Estate L. T. & T. Co.*, 297 U. S. 606, this Court reversed the judgment of the Circuit Court of Appeals for the Third Circuit on the sole ground that the Circuit Court had failed to follow the District Court's finding that a gift had been made in contemplation of death. It was there said (p. 608):

> "The instant case is controlled by the established rules relating to appellate review in actions at law where a jury trial has been waived. R. S. 649, 700; 28 U. S. C. 773, 875. Where a general verdict is found by the trial court, it has the same effect as the verdict of a jury. The appellate court cannot pass upon the weight of evidence. * * * The ultimate question for the decision of the trial court was one of fact and its general verdict was conclusive. The Circuit Court of Appeals was without authority to weigh the evidence and to make its own findings."

This decision was recently cited with approval by this Court in *Allen* v. *Trust Company of Georgia, et al,* October Term, No. 289, decided January 28, 1946.

In *Tennessee Coal Company* v. *Muscoda Local,* 321 U. S. 590, decided subsequent to the adoption of Rule 52 (a), this Court recently considered the binding effect of the District Court's finding of fact with respect to the alleged existence of a custom in the coal mining business for the payment of wages during underground travel. It was there said by Mr. Justice Murphy (page 602):

> "We thus cannot say that the District Court's findings as to custom and contract are so clearly erroneous as to compel us to disregard them."

In *Commissioner of Internal Revenue* v. *Scottish American Investment Company, Ltd.,* 323 U. S. 119, this

Court, speaking again through Mr. Justice Murphy, made the following statement, which is particularly pertinent in the instant cases (page 124):

> "The Circuit Courts of Appeal have no power to change or add to those findings of fact or to reweigh the evidence. And when the Tax Court's factual inferences and conclusions are determinative of compliance with statutory requirements, the appellate courts are limited to a determination of whether they have any substantial basis in the evidence. *The judicial eye must not in the first instance rove about searching for evidence to support other conflicting inferences and conclusions which the judges or the litigants may consider more reasonable or desirable.* It must be cast directly and primarily upon the evidence in support of those made by the Tax Court. If a substantial basis is lacking the appellate court may then indulge in making its own inferences and conclusions or it may remand the case to the Tax Court for further appropriate proceedings. But if such a basis is present the process of judicial review is at an end." (Emphasis supplied.)

In the instant cases the evidentiary facts were supplied by a stipulation and the testimony of one witness. As shown by the decision of this Court in the *Scottish American* case, *supra,* the conclusion of ultimate fact as to the intention of the parties by the District Court, is in itself a fact which cannot be disturbed unless clearly erroneous. The Circuit Court's misconception as to the conclusive nature of the District Court's findings based upon the undisputed evidentiary facts is apparent from the following statement in its opinion (App., p. 18a):

> "There were no conflicts of testimony to be resolved at the trial. Most of the facts were stipulated and the testimony of the one witness, A. G. Scattergood,

> Vice-President of the plaintiff, was not disputed but relied on by the defendant. Our question becomes, therefore, what is the legal conclusion to be drawn from facts rather than what are the facts themselves."

. It has been held by this Court that, insofar as the binding nature of the findings of fact are concerned, there is no difference between those which are based on stipulation and those which are based upon disputed testimony. Thus, in *Boehm* v. *Commissioner of Internal Revenue,* 90 L. ed. 96 (not yet reported officially), the following statement was made (p. 100):

> "The circumstance that the facts in a particular case may be stipulated or undisputed does not make this issue any less factual in nature. The Tax Court is entitled to draw whatever inferences and conclusions it deems reasonable from such facts. * * * If it is in accordance, [with law] it is immaterial that different inferences and conclusions might clearly be drawn from the undisputed facts."

The foregoing opinions by this Court in the *Scottish American* case and in the *Boehm* case were rendered in deciding appeals from the Tax Court. However, since in such cases the findings can be disregarded if they do not have "any substantial basis in the evidence", those decisions can be applied equally well under Rule 52 (a) where the finding is conclusive unless "clearly erroneous". In *National Mutual Casualty Co.* v. *Eisenhower,* 116 F. (2d) 891 (C. C. A. 10th, 1940) the Circuit Court of Appeals for the Tenth Circuit adopted the same reasoning under Rule 52 (a) as this Court applied in the *Scottish American* case. It was there said (p. 894):

> "Contradictions and conflicts of evidence are for the trier of the facts, whether it be court or jury, and where the evidence and the inferences fairly deducible

> from it are such that reasonable minds may honestly draw different conclusions from them, it has been held by this court that the question is not one of law, but of fact, to be determined by the trier of the facts."

It does not clearly appear from the opinion of the Circuit Court of Appeals whether that Court considered the question one of fact or of law. At one point, as has been seen, the Court treated the issue as a factual one, and at another point it considered only the wording of the assignments apart from the surrounding circumstances, thus implying a legal question solely. However, the Circuit Court of Appeals was not at liberty to nullify the effect of the Trial Court's finding by considering it in any light other than as a finding of fact.

It has long been held that the giving and execution of contemporaneous agreements, under circumstances which indicate that the parties intend to achieve a different result thereby than that apparent on the face of the instruments, makes the interpretation of the contemporaneous agreements a question of fact to be decided by the jury or by the judge, if sitting alone, as in this case.

The most revealing case on this subject is *Bogk* v. *Gassert,* 149 U. S. 17, decided by this Court in 1893. In that case two deeds, an agreement to reconvey, and a lease, all for the same land, were executed simultaneously by the parties. The suit was on the lease. The other contemporaneous agreements were put in evidence by the defendant along with other evidence as to the intention of the parties, asserting that the whole disclosed that the parties had intended a mortgage. This Court there said (page 29):

> "The case was evidently a proper one to go to the jury, who were left to determine the question whether the instruments were *intended* as a mortgage, and were instructed that, if they found them to be such, the plaintiffs could not recover." (Emphasis supplied.)

The foregoing rule also applies in Pennsylvania. Thus, in *Harper's Appeal,* 64 Pa. 315, it was held by the Pennsylvania Supreme Court that *the finding by the Trial Judge* that an absolute deed accompanied by a separate instrument, in which the grantee agreed to reconvey the property at the grantor's request within three years, was intended to have the effect of a mortgage, would not be disturbed on appeal without a conclusive showing to the contrary. It was there said (page 319):

> "Accepting the opinion of the court below as the report of a master upon the evidence, we see no plain mistake in the conclusion at which they arrived, that the agreement of March 19th 1858 was cotemporaneous with the deed of March 18th 1858, from Gubbings and wife to Harper. Without very clear and persuasive evidence that the sale was an absolute one, and the agreement to reconvey a subsequent, distinct and independent contract, we must treat the transaction as a mortgage. Such, undoubtedly, is the result of the authorities in this state: Colwell *v.* Woods, 3 Watts 188; Kerr *v.* Gillmore, 6 Id. 405; Jaques *v.* Weeks, 7 Id. 261; Brown *v.* Nickle, 6 Barr 390; Reitenbaugh *v.* Ludwick, 7 Casey 131; Wilson *v.* Shoenberger's ex'rs., Id. 295."

Likewise, in *Herman* v. *Pepper,* 311 Pa. 104, 166 Atl. 587, the Pennsylvania Supreme Court did not disturb *the finding of a Court of Equity* that an assignment of a partner's interest, absolute on its face but in fact given as security for a loan and accompanied by a separate agreement to reassign upon payment thereof, was in fact a pledge.

See also *Huston* v. *Regn,* 184 Pa. 419, 39 Atl. 208; and *McCollum* v. *Braddock Trust Company,* 330 Pa. 293, 198 Atl. 803.

The instant case is indistinguishable in principle from *Bogk* v. *Gassert, supra,* and the other cases cited above.[2] The bonds, assignments thereof and consents were executed contemporaneously. In fact, the assignments and consents were executed in advance of the time that the bonds became effective by delivery. Under such circumstances the intent of the parties was a fact to be determined by the trial court from all the circumstances, and, once having been determined, the Circuit Court of Appeals was not at liberty to set it aside unless clearly unsupported by evidence.

In *Biggs* v. *Mays,* 125 F. (2d) 693 (C. C. A. 8th, 1942), the Circuit Court of Appeals for the Eighth Circuit considered itself bound to follow Rule 52(a) in a case similar to the instant ones. In that case the question was whether the acts and words of a debtor constituted a promise to pay which had tolled the running of the Arkansas statute of limitations, a question of fact under the Arkansas law. The Court said (p. 699):

> "The court below found specifically that 'the facts do not justify any inference of a promise to pay the note as demanded by the claimant.' Under the law of Arkansas, as outlined above, the inference of a promise to pay *is one of fact,* and the finding of the court is binding unless clearly erroneous. Rule 52(a) of the Rules of Civil Procedure, 28 U. S. C. A. following section 723c."

In the instant case in arriving at its determination that the parties intended merely an ordinary assignment, the Circuit Court of Appeals for the Third Circuit ignored the following Federal Rules: (A) That an appellate court shall not draw its own conclusions and inferences from the evidence; (B) That findings based on

[2] The Circuit Court appears to have disregarded the principle of these cases in the mistaken belief that the decisions were based upon reliance upon superior skill, mistake or domination of one party by the other. That such is not the case is apparent from even a cursory reading of the opinions.

undisputed facts are as conclusive as those based on disputed ones; and (C) That a finding of fact shall not be set aside unless clearly erroneous.

Thus, we have here a situation in which the Circuit Court of Appeals has disregarded an express finding of fact by a District Court, supported by substantial evidence, which fact is not only relevant but is determinative of the issues involved in these cases. The writ should issue to correct this abuse of appellate review.

The Construction Placed Upon the Conditions of the Bonds by the Circuit Court of Appeals is in Conflict with Applicable Pennsylvania Decisions.

The Circuit Court of Appeals based its decision as to the proper interpretation to be placed upon the condition in the bond on the following statement of what it considers to be the law of Pennsylvania (Appendix, p. 22a):

> "If the Young case (Young *v.* American Bonding Company, 228 Pa. 373, 77 Atl. 623) is in point, we think it establishes the proposition that the words used in this type of bond which, in turn, contains a reference to a contract, makes performance of the surety's promise conditioned upon the non-performance of the main contract by the principal debtor."

Following this statement of its concept of the law of Pennsylvania, the Court held that the condition of the bond should be construed in the light of the terms of the contract mentioned in the recital. Hence the failure of the nominal obligee to perform under the contract constituted a defense for the surety.

This statement of the law is correct only if the reference to the contract appears in the *condition* of the bond. It is totally incorrect if the reference to the contract appears merely *in a recital* of the bond, as in these cases.

The recitals and the condition of each bond in the instant cases are as follows:[3]

"WHEREAS, the Principal has entered into a written agreement dated the 15th day of October 1928, with the Equitable Bonded Mortgage Company for the erection and completion of twenty (20) dwellings on Southeast side of Wadsworth Avenue, between Anderson Street and Ardleigh Street, 22nd Ward, City of Philadelphia, in accordance with certain plans and specifications duly signed and approved by all parties interested; and

"WHEREAS, the Equitable Bonded Mortgage Company has agreed to advance One Hundred Forty-two Thousand Dollars ($142,000.) for the purchase of, and to be secured by assignments of first mortgages on the above mentioned dwellings, and

"WHEREAS, the Equitable Securities Corporation has agreed to advance Eighty-one Thousand Dollars ($81,000.00) for the purchase of, and to be secured by assignments of second mortgages on the above mentioned dwellings.

"NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION IS SUCH, That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to, and herein incorporated with like force and effect as if attached hereto, free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect."

Certain things should be noted about this bond preliminarily. The first recital refers to two different things.

[3] The only differences between the bonds are the names of the builders, the amounts involved, and the location of the property.

The first is a contract between the builder and Equitable for the construction of the dwellings, and in which Equitable promised to pay the builder. The second is the plans and specifications according to which the houses were to be built. The condition is that the buildings shall be built—*not in accordance with the contract,* but—*in accordance with the plans and specifications,* which are expressly incorporated as if attached thereto.

It is, of course, obvious that the extent of the undertaking of the principal and surety in any bond is the condition of the bond. The prefacing of the condition by recitals is usually only for the purpose of setting forth the background for the condition.

In Pennsylvania the Courts look to the recitals of a bond to explain the condition thereof only in certain types of cases. Thus, if the condition is so indefinite as to be unenforceable, the Court will resort to recitals in order to clarify the condition: *United States* v. *Morrisdale Coal Co.*, 50 Fed. Supp. 138 (D. C. E. D., Pa., 1942); or if the basic contract, for the performance of which the bond is really given, is set forth in complete detail in a recital, the Court will interpret the condition in the light of the contract so set forth: *Nazareth F. & M. Co.* v. *Marshall Co.*, 258 Pa. 558, 102 Atl. 268.

It is readily apparent that the instant case does not fall within either of the foregoing categories. Thus, the recital merely mentions the existence of the builder's agreement and there is no attempt to set forth in detail any of the terms of that agreement. Nor can it be said by any stretch of the imagination that the condition of the bond is so indefinite as to need explanation or amplification by the recitals in the bond.

There is one last exception to the general rule that the condition of the bond alone measures the liability of the parties thereto. That exception is the one which the Circuit Court of Appeals in these cases has mistakenly applied as a general rule. There are two cases which

give rise to this exception. One is the *Young* case, cited by the Circuit Court, and the other is *Dunbar* v. *Fleisher*, 137 Pa. 85, 20 Atl. 520. To show the genesis of this exception, and thereby clarify the decision in the *Young* case, the holding of the Pennsylvania Supreme Court in *Dunbar* v. *Fleisher* will be considered first. In that case the defendant, Fleisher, was surety on a bond for the faithful performance by two men, Harper and Famous, of certain masonry work *"as per contract"* between those two men and the plaintiff.[4] The said Harper and Famous did not perform the masonry work and this action was against the defendant on his surety bond. The defense was that payments required to have been made to Harper and Famous by the plaintiff had not been made and that therefore the defendant was relieved of his obligation, the same defense which the defendant has raised in this case. It was there held by the Supreme Court of Pennsylvania, in affirming judgment for the defendant, that the defense of non-payment under the terms of the principal contract was properly raised since *the condition* of the bond expressly referred to that contract.

Young v. *American Bonding Company, supra,* is the same as the *Dunbar* case. In the *Young* case the bond in suit was also a construction bond. It recited the existence of the contract under which the construction improvements were to be made, and was conditioned upon the faithful completion of those improvements *"as provided in said agreement"*.[5] The Supreme Court of Pennsyl-

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4 "Whereas, J. R. Dunbar has this day given to Jesse Harper and John Famous an order on the county commissioners for $62, or the amount that shall be due them for mason work at the completion of the bridge in Penn township, Perry county, Pennsylvania. Now, in consideration of $1 to me in hand paid, I hereby become security for said Harper and Famous for the faithful performance of said mason work to said bridge, *as per contract* with said J. R. Dunbar." (Emphasis supplied.)

5 "Now therefore the condition of this obligation is such that if the said principals shall well and faithfully construct and complete said improvements of the value of Three Hundred and Fifty Thousand Dollars ($350,000) upon said property, *as provided in said agreement*, on or before the 31st day of December, 1906, then this obligation to be null and void; otherwise it shall remain in full force and effect." (Emphasis supplied.)

vania again held, and properly so, that the undertaking of the surety, as shown by the condition of the bond, was subject to the terms of the agreement since the condition expressly referred to that agreement.

The reason behind the decisions in the *Young* case and the *Dunbar* case is plain. The condition of the bond was that certain things be done in accordance with a contract, and therefore the contract became a part of the condition. It is merely a specific application of an elementary rule of interpretation.

In the instant cases, unlike the *Young* case and the *Dunbar* case, however, *the condition* of the bond makes no reference to the agreement between the builder and the promoter. It is only in the recital that the contract appears at all. To hold, as the Circuit Court did in these cases, is to build one exception to the general rule on top of another exception, that is, to construe a clear condition needing no explanation in the light of a contract mentioned only in a recital and not even referred to in the condition.

The strained nature of this interpretation is particularly apparent from the fact the parties showed clearly that they knew how to incorporate by reference. The condition is that the houses shall be built by either the builder named in the bond or by the surety "in accordance with *the plans and specifications* above referred to, and herein incorporated with like force and effect as if attached hereto". By applying the common-sense rule of *expressio unius est exclusio alterius* it is evident that the parties intended that the contract should *not* be a part of the condition.

The decision of the Pennsylvania Supreme Court in the case of *Purdy* v. *Massey,* 306 Pa. 288, 159 Atl. 545, states the law clearly applicable here. Due to the fact that certain phases of that case are so similar to the ones in the instant case, it is felt that the following detailed

discussion is merited.[6] In that case the owner of land had entered into a written agreement with the builder for the construction of a garage in accordance with detailed plans and specifications. The plaintiff agreed to subordinate her first mortgage on the land to a new mortgage, the proceeds of which were to be used to finance the construction. In return for subordinating her first mortgage, the plaintiff asked for, and received, a surety bond which, after reciting the existence of the construction agreement between the builder and owner, contained the condition that provided the builder should "complete the buildings mentioned free and clear of mechanics' liens or claims, then this obligation shall be void; otherwise to be and remain in full force and effect". The garage was never built and this suit was upon the bond against the builder and the surety. After judgment for the plaintiff in the Trial Court, the defendant surety appealed, and one of its assignments of error was that the Trial Court had refused to charge that there was no default on the part of the builder since the builder had never received the money payments required by the contract, the same defense as in the present cases. This assignment of error was overruled by the Pennsylvania Supreme Court and the judgment of the Court below was affirmed. The Court held that the undertaking by the defendant surety was an absolute one for the construction of the garage, and that the terms of the contract did not enter into the interpretation of the bond condition. It said:

> "The covenants in a bond 'should be construed to mean what the parties intended in so far as that intention can be ascertained by the words used': Equitable Trust Co. *v.* National Surety Co., *supra*. If, however, the language is not free from doubt, then the circumstances surrounding the making of the bond, and particularly the purpose for which it was given,

[6] The information appearing in this discussion which does not also appear in the printed report of the case, was obtained from the original record.

should be taken into account: March *v.* Allabough, 103 Pa. 335; Ambridge *v.* P. & B. St. Ry. Co., 234 Pa. 157. In this case such considerations lead to but one conclusion—*that this bond was an absolute undertaking to erect and complete the building.*

"This bond is to be construed most strictly in favor of the plaintiff. The obligor, Indemnity Insurance Company of North America, is a paid surety engaged in the business of furnishing bonds for profit; we have frequently held that in cases of corporate sureties, the bond is to be strictly construed in favor of the obligee: Young *v.* American Bonding Co., 228 Pa. 373; South Philadelphia State Bank *v.* National Surety Co., 288 Pa. 300, and cases there cited.

"*The condition of the bond is performance of a specific thing—completion of the building provided for in plans and specifications made a part of the bond—and the only alternative for performance is the bond itself.* It is obvious, being clearly expressed by the words of the bond and the circumstances surrounding the transaction, that the intent of all concerned was to give plaintiff in lieu of her first mortgage the enhanced value of the real estate by the addition of the building, or failing that, its equivalent in money—not to exceed the face value of the bond." (Emphasis supplied.)

The decision in the *Purdy* case is clearly in point here. The recital mentioned the builder's contract, the condition did not, and the court held that the bond was an absolute undertaking that the structure be built. Furthermore, it can be said with equal force in this case that the purpose of the bond was to give Petitioner "the enhanced value of the real estate by the addition of the building, or failing that, its equivalent in money."

It will be noticed from the decision of the Court in the *Purdy* case that if the language of the bond is not free from doubt "then the circumstances surrounding the making of the bond, and particularly the purpose for which it was given, should be taken into account". The Petitioner believes that the language is clear and unambiguous, but since the Circuit Court of Appeals did not, or otherwise it would not have resorted to the contract, it should have followed the findings of fact by the District Court. That Court considered the case as one requiring an examination of the surrounding circumstances and found as follows (App., p. 8a):

> "So considered I find that the bond in this case was an absolute undertaking by the defendant directly to the plaintiff that the houses would be completed according to plans and specifications identified by reference to the operation agreement, that it was intended solely to secure the plaintiff's loan and was not intended to and did not guarantee full performance of the operation agreement, that it was not intended to and did not confer any rights (except contingently on full payment to the plaintiff) upon Equitable or its subsidiary, that the plaintiff was the real obligee and that no default on the part of the nominal obligees would affect the plaintiff's rights."

Since the Circuit Court of Appeals believed that the language was ambiguous, it was no more at liberty to disregard the District Court's finding in this particular than it was as to the parties' intent in making the "assignment" (see *supra*, pp. 13-16).

The discretionary power of this Court may be invoked to grant a writ of certiorari when a Circuit Court of Appeals has made an error in interpreting an important question of local law. The importance to the Petitioner of the error in these cases can be seen from the fact that

the judgments in these companion cases total almost a million dollars. The importance of the decision to those dealing with surety bonds in Pennsylvania can also be seen from the fact that the door has been opened now to interpretation in the light of any and all recitals unless it is expressly stated that they are *not* a part of the condition. If that is to be the law, when heretofore only the contrary was true, a great deal of the collateral held by financial institutions in Pennsylvania has decreased in value over night. This Court should exercise its power to review these cases and set at rest the doubts created by the Circuit Court of Appeals' decision.

The Rule, Sustained by Pennsylvania Decisions and Decisions of This Court, that the Contracts of Paid Sureties Are to Be Construed Strictly Against Them, Has Not Been Followed by the Circuit Court of Appeals in These Cases.

It is a settled rule in Pennsylvania, as it is throughout this country generally, that the contract of a paid surety will be construed most strongly against the surety and that all doubts and technicalities arising in said undertakings will be resolved in favor of the obligee. A typical statement of this rule appears in *Mechanics Trust Co.* v. *Fidelity & Casualty Co.*, 304 Pa. 526, 156 Atl. 146, where it was said (p. 533):

> "We have frequently said that the trend of modern decisions, federal and state, has been to distinguish between individual and corporate suretyship, where the surety has undertaken, for money, the contract of suretyship which it is its business to sell; in such cases, the contract should be construed most strictly in favor of the obligee: South Philadelphia State Bank *v.* National Surety Co., 288 Pa. 300, 305-6, and cases there cited."

See also, *Monongahela Street Railway* v. *Philadelphia Co.*, 350 Pa. 603, 617, 39 A. (2nd) 909; *Fiumara* v. *American Surety Co.*, 346 Pa. 584, 595, 31 A. (2nd) 283; *Hess* v. *Merion Title & Trust Co.*, 317 Pa. 501, 505, 177 Atl. 53; *Sokoloff* v. *Fidelity & Casualty Co. of N. Y.*, 288 Pa. 211, 215, 135 Atl. 746.

In spite of this well established rule of construction, the Circuit Court of Appeals construed the bonds in suit in favor of the paid surety. In fact, it may well be said that the Court treated the Respondent as though it were a volunteer surety, a favorite of the law.

The Petitioner does not believe that the language of the bond need be strained to be construed against the Respondent Surety in order to hold that the condition of the bond is absolute for the building of the houses. It is submitted that the mere reading of the bond itself, without construing it expressly in favor of one party or the other, leads inevitably to that conclusion. On the other hand, however, the Petitioner is aggrieved by the obvious fact that the condition of the bond was construed against it, an assured, and in favor of the Respondent, a paid surety.

It was the business of the Respondent to insure the undertakings of other persons. It is experienced and, presumably, normally efficient in this business. If the Respondent had intended originally that its obligation to construct the dwellings should be dependent upon the performance of the building contract between the builder and the promoter, it could have protected itself by inserting a reference to that contract in the condition of the bond, or by merely guaranteeing the performance of that contract. The surety disclosed in the condition as written the fact that it knew how to incorporate extraneous documents into the condition of the bond, for it did so as to the plans and specifications for the dwellings which, like the contract, were referred to in the recital. In the face of this demonstration of skill in draftsmanship, one must

be most solicitous of the welfare of the surety to conclude that the contract was also incorporated in the condition.

Only by distorting the language of the instrument is one able to reach the conclusion, achieved without apparent difficulty by the Circuit Court of Appeals, that the Respondent Surety had premised the performance of its undertaking upon the accomplishment by the promoter of all the many acts required of it in its contract with the builder. If clear and unambiguous language is to be perverted by "interpretation", let that be done for the benefit of the innocent lender, and not for the gain of the paid surety.

The ultimate effect of favoring the surety in this instance is stated by the District Court (App., p. 7a):

> "To sustain it (the Respondent's contention) would result in giving to Equitable, which received the plaintiff's money and which was one of two parties ultimately to benefit by it, a status which would allow it to dissipate the money or appropriate it to its own purposes, and by doing so, at one and the same time prevent completion of the houses and destroy the plaintiff's right to realize upon its security. To state that proposition, it seems to me, is to answer it."

The Circuit Court of Appeals, by its decision in this case, manifestly has accorded to Respondent Surety a position completely at variance with the one to which it is entitled under the general rule. The Court has therefore misapplied, and not merely failed to apply, an important rule of Pennsylvania law.

The principle that contracts of paid sureties will be construed against them was called to the attention of the Circuit Court of Appeals by counsel for Petitioner by citing the case of *Baglin* v. *Title Guaranty & Surety Co.*, 166 Fed. 356; affirmed 178 Fed. 682 (C. C. A. 3rd, 1909). This authority was summarily disposed of by the Circuit

Court of Appeals in the following footnote to its opinion (App., p. 16a):

> "The decision referred to by appellee as presenting a case (Baglin *v.* Title Guaranty Surety Co., 166 Fed. 356, affirmed 178 Fed. 682 (C. C. A. 3, 1909)) 'so nearly identical' was decided long before Erie R. Co. *v.* Tompkins was ever dreamed of. A Federal Court decision upon a question of state law settled upon principles of 'general commercial law' is no precedent now."

A careful reading of the opinions in the *Baglin* case would clearly show that these opinions state not only the general law applicable to the defense of a paid surety, but record the then and present law of Pennsylvania—all contrary to the different and new law now made by the decision of the Circuit Court of Appeals herein complained of. The following quotations from the *Baglin* case show how erroneous the footnote is:

By Judge McPherson (166 Fed. 363):

> "Nor is there any reason to be astute in looking about for flaws that may invalidate the transaction. The defendant is not entitled to the tender consideration that is accorded to an individual surety who is a mere volunteer. Surety companies are not to be so described; they are insurers, paid for their services, bound by contracts which are usually carefully drawn by themselves, and, as a general rule, satisfactorily secured by counter indemnity. They perform a most useful, and indeed, according to modern custom, an indispensable, function in the business and legal world, but they differ so much from an individual surety of the ordinary type as to render inapplicable some of the reasons that have led the courts to guard the rights of the individual surety with jealous care."

By the Circuit Court of Appeals, affirming (178 Fed. 687):

> "* * * The bond sued upon is not an indemnity bond. Defendant is bound, as surety or guarantor, to the plaintiff, as obligee in the bond, and, in the words of the trial judge, 'the fact remains that the guarantee in question was given and paid for; that it warranted the performance of a lawful act, and that such act has not been performed,' and by its nonperformance, defendant's liability is fixed."

Petitioner respectfully submits that if a new rule of law is to be established now by judicial fiat, to relieve a paid surety from its contract obligations, it should be established by a decision of this Court, after full consideration, and not by the Circuit Court of Appeals for the Third Circuit.

The Decision of the Circuit Court of Appeals Contains Such a Fundamental Inconsistency That it Constitutes a Serious Departure From the Usual Course of Judicial Procedure.

As has been seen, the Circuit Court of Appeals judged this case from two aspects. First, it considered whether the transaction was an assignment of the bond which would permit the Respondent Surety to raise a defense against the Petitioner which it would have had against the nominal obligee, or whether it was a direct obligation to Petitioner. Secondly, it considered whether the bond was an absolute undertaking, or whether the condition of the bond was itself conditioned upon the performance of the building contract. In the first instance, the Court held that the transaction was an ordinary assignment; and, in the second instance, it determined that the condition of the bond was modified by the terms of the building contract.

In deciding that the Petitioner was merely an assignee of the bond, the Court said that the language used in the instrument was not ambiguous and that therefore it would not consider the surrounding circumstances in determining the intent of the parties. However, in construing the condition of the bond, the language of which is certainly as clear and definite as that of the assignment, the Court read into it the terms of the main contract between the nominal Obligee and the Obligor Builder, which contract was not even referred to in the condition.

Despite the fact that the Circuit Court of Appeals stated in its opinion that "the rule that contracts mean what they clearly say applies to both contracting parties", the Court nevertheless applied a rule of strict construction to the benefit of the paid surety in one phase of the case; and, in the other phase of the case, in which the rule of strict construction should have been applied, it chose to adopt a liberal and strained construction, also to the benefit of Respondent Surety.

If the Circuit Court of Appeals had consistently applied the first rule which it employed, namely, that only the exact language of the contract will be considered, it would necessarily have had to find that the condition of the bond was absolute for the construction of the dwellings in any event. Nothing could be more certain or unambiguous than the covenant in the bond that "if the buildings hereinabove mentioned shall be fully constructed and completed * * * free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect".

On the other hand, if it had applied throughout the second rule which it adopted, namely, that matters extraneous to the agreement may be considered in interpretation, it would have followed the finding of fact by the District Court that the surrounding circumstances showed the parties intended an absolute undertaking by the Builder and Respondent Surety directly to Petitioner.

It is disturbing to find that the Circuit Court of Appeals adopted this inconsistent attitude in the face of the fundamental rule that the contracts of paid sureties shall be construed strictly against them.

The rationalization by the Circuit Court of Appeals of this obvious inconsistency to the benefit of the Respondent Surety might possibly be said to be based on a misconstruction of the decision of the Pennsylvania Supreme Court in *Young* v. *American Bonding Company, supra,* and a further misconstruction of the general rule as to the proper mode of interpretation of contemporaneous instruments. However, two wrongs do not make one right. Either the Court should have applied the rule of strict construction throughout, and in doing so found that the condition of the bond was absolute; or it should have held that the circumstances of the transaction were relevant and affirmed the judgment of the District Court on its findings of fact.

The fundamentally inconsistent reasoning applied by the Circuit Court of Appeals in these cases, to the benefit of the Respondent Surety and to the great pecuniary harm of the Petitioner, who advanced money in reliance upon Respondent Surety's promise, is so great that it constitutes a departure from the usual course of judicial procedure. If "the rule that contracts mean what they clearly say applies to *both* contracting parties", then this Court should grant a writ of certiorari so that that rule may be enforced.

CONCLUSION.

It is submitted that the Circuit Court of Appeals, by its decision in these cases, has violated Rule 52(a) of the Federal Rules of Civil Procedure and the decisions of this Court interpreting that Rule.

In addition to having rendered a decision in conflict with the decisions of this Court, the Circuit Court of

Appeals has also created new rules in Pennsylvania as to very important phases of the law of surety bonds. Heretofore the undertakings of paid sureties, although subject to interpretation, had a certainty to them which made them desirable as security in the field of both private and public enterprise. Furthermore, if the extent of the obligation proved indefinite in the light of future events, the assured could place reliance upon an interpretation in keeping with the underlying purpose of the bond and a favored position as opposed to a paid surety. The decision of the Circuit Court of Appeals, here complained of, has upset this long-standing condition, on the basis of which great numbers of bonds have been accepted as guaranties of the performance of an endless variety of undertakings. This decision has cut at the very roots of suretyship in Pennsylvania.

For the reasons stated, it is earnestly urged that the Writ of Certiorari, herein prayed for, be granted, and that the decision of the Circuit Court of Appeals for the Third Circuit be reviewed and reversed.

Respectfully submitted,

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APPENDIX.

OPINION.

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

No. 15270. March Term, 1930.

Provident Trust Company of Philadelphia

v.

Metropolitan Casualty Insurance Company of New York.

(Filed June 8, 1944.)

Before (s) KIRKPATRICK, *J.*

This is one of two civil actions which were tried together to the Court without a jury. The two actions are against a surety company and are based upon three bonds of a type commonly known as completion bonds, given in connection with three building operations, referred to respectively as the Furman, Roehm and Storck operations, those being the names of the three builders. The bonds are essentially alike and the two cases present the same questions of law, the only difference being that in the first case (Furman and Roehm bonds) the plaintiff sues in its individual capacity and in the second case (Storck bond) as trustee. As a matter of convenience the Furman operation will be considered, it being understood that the discussion, except as noted, applies equally to the other two operations.

The operation was undertaken by, or through the medium of, a corporation named Equitable Bonded Mortgage Company which, with a wholly owned subsidiary, Equitable Securities Corporation, was in the business of financing such operations, either by purchasing mortgages on the lots upon which houses were to be built or by lending money upon the security of such mortgages. The financing in this case was accomplished by means of the following (apparently) successive steps:

(a) A contract between the builder and Equitable, called an "operation agreement" which provided, among other things, that mortgages would be placed upon 20 of the lots, that a house would be constructed upon each according to agreed plans and specifications, that the mortgages would be transferred to Equitable and that Equitable would supply the money to the builder as the work proceeded. (b) The creation of the mortgages by the builders and their delivery to Equitable. (c) A bond given by the builder as principal, with the defendant as surety, to Equitable and its subsidiary for the completion of the houses. (d) Tender by Equitable to the plaintiff of its note in the amount of $112,000, the 20 mortgages, assigned to the plaintiff, and the defendant's surety bond assigned by Equitable to the plaintiff, accompanied by the defendant's written consent to the assignment. (e) The advance by the plaintiff to Equitable of $112,000.

The operation agreement, the mortgages and the assignments of them to Equitable and by Equitable to the plaintiff, the defendant's bond, its assignment by Equitable to the plaintiff, and the defendant's consent thereto all bear the date of October 15, 1928, and, as a matter of fact, the whole transaction was consummated on that day, except that the plaintiff advanced the money from time to time as required. Before (Stipulation Par. 3) the defendant's bond was delivered to Equitable, an assignment of it by Equitable to the plaintiff had been executed and the defendant had placed its written consent upon the instrument of assignment. The bond and assignment, with a statement of the defendant's financial condition and a power of attorney authorizing the execution of the bond, were bound together and backed by a single office backer of the defendant. In that form they were presented to the plaintiff together with the mortgages and Equitable's note.

It is undisputed that the houses were never completed (in fact, they were scarcely begun) that Equitable's note is unpaid and worthless, that the plaintiff realized the sum

of $150 from the sale of the mortgages, that no recovery can be had from the builder, that had the houses been completed the plaintiff would have been amply protected and that unless the plaintiff can hold the defendant upon its bond it will lose most of its loan.

The bond names Equitable and its subsidiary as the obligees. It recites and identifies the operation agreement between the builder and Equitable and the agreements of Equitable and its subsidiary to advance money for the work to be secured by assignment of first and second mortgages on the houses. The condition is as follows, "That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to, and herein incorporated with like force and effect as if attached hereto, free and clear if (sic) mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect."

The surety's defenses are:

1. That the builder having been excused from performance by Equitable's default in failing to advance money for the buildings as it had agreed to do in the operation agreement and the principal therefore not being liable, the surety could not be held by Equitable, and hence cannot be held by the plaintiff, which, the defendant says, is nothing more than an assignee of a defaulting obligee, with rights no broader than those of its assignor. Note. It is an undisputed fact that Equitable never advanced any money to the builder for the construction of the houses, and it may be accepted as a fact that that was the reason the houses were not built and that, as between himself and Equitable, the builder would have been excused from performing by the failure of Equitable to advance the money or, as the defendant describes it, failure of consideration.

2. That Equitable and its subsidiary are joint obligees, and that default on the part of the subsidiary, the second

mortgage, which did not join in the assignment of the bond to the plaintiff is fatal to the rights of Equitable or any assignee of Equitable, regardless of any rights which the plaintiff might still have, had Equitable been the only obligee.

3. That the plaintiff lost its rights against the surety, because

(a) Its sale of the mortgage after default carried the right to recover on the surety bond, which, the defendant says, was given as security for the mortgages only, and so the sale divested the plaintiff of all further interest in the surety bond.

(b) The subsequent satisfaction of the mortgages paid the debt and released the surety.

(c) The renewal, before default, by the plaintiff of Equitable's six months note for a further period of six months, was an extension of credit which released the surety.

4. That the plaintiff has failed to prove damages.

5. That the plaintiff has lost its rights by abandonment and delay in prosecution.

At the center of the entire controversy, decisive of the issue raised by the first two defenses and directly affecting the third and fourth, lies the question whether this is a bond for the faithful performance of a contract (the operation agreement) or a bond for the completion of houses. If the former, the position taken by the surety in its first two defenses has, at least, technical merit. If the latter, it has none at all.

The defendant relies upon Young *v.* American Bonding Co., 228 Pa. 373. In that case the condition of a bond in terms similar to but not identical with those in the present case was construed in connection with the recitals (which referred to portions of a contract roughly corre-

sponding to the present operation agreement) to cover the faithful performance of the entire contract, including details of financing, and the Court held that a material alteration to the detriment of the surety in some of the financing provisions released the surety.

I do not think that Young *v.* Bonding Co. rules the present case.

The difference in the wording of the conditions of the two bonds may be noted. It is slight but not entirely without significance. In the Young case the condition was, "if the said principals shall well and faithfully construct and complete . . .." In the present case the condition is, "That if the buildings hereinabove mentioned shall be fully constructed and completed . . .."

But regardless of similarities or dissimilarities in the two bonds, the evidence shows that the transactions of the Young case and the present case, of which the bonds in the two cases formed part, were fundamentally entirely different, a fact which compels a different construction of the condition of this bond.

There is no doubt about the principle of the Young case that the recitals of a bond may properly be referred to in order to ascertain the scope of the condition. But the recitals are not always conclusive, and the Young case does not decide that they are. In construing the condition of a bond, the circumstances, including the nature of the transaction as a part of which it was given, are to be taken into account. If, when the entire transaction is considered, it appears indisputably that the intention was to give the surety's absolute undertaking, disassociated from other contract obligations, that certain buildings would be completed then the condition must be so construed, though the recitals contain a reference to the other provisions of the contract. This, I think, is what appears in the present case.

I have described the form in which the transaction was cast. The substance of it was this:

Equitable and the builder, for their mutual profit, proposed to engage in a venture, consisting of the building of houses, for which money, in the amount of $112,000, was needed. It was found to be necessary, convenient or desirable to borrow from the plaintiff, which was willing to lend the money on the security of the land if, and only if, it could be assured by a corporate surety bond that houses would be built upon the land and completed in accordance with the plans. The plaintiff had no interest whatever in who got the money or how it was used. If the bond was adequate and the obligation honored, nothing the parties to the operation agreement might do or fail to do would affect the security of the loan. The defendant executed its bond with the condition that the houses would be built. The defendant knew the money for the operation was coming from the plaintiff and that the bond was going to be offered as security. And it must have known, from the dates which the documents bore and the fact that its bonds was delivered to Equitable already assigned to the plaintiff, if from nothing else, that the transaction was not and was never intended to be a series of distinct steps but was simply a borrowing from the plaintiff upon collateral which included the bond. With this knowledge it accepted the premium and delivered the bond, upon the faith of which, primarily, the plaintiff advanced the money.

Only on paper was Equitable ever an obligee. It never took anything but a remote and contingent interest in the bond, an interest which could attach only after the plaintiff had been paid in full, and, as a matter of fact, that never happened. Its position, if it be necessary to assign it a position, was in reality that of principal along with the builder. The subsidiary was Equitable's creature, and the legal fiction of a separate corporate existence for it cannot change the realities of the situation. It would be idle to pretend that Equitable's acts were not the acts of the subsidiary and that, so far as the plaintiff in this transaction was affected, the two corporations were not one and the

same. (Defendant's fifth request for finding of fact, affirmed by the Court.)

The defendant's position is a stand upon the technical aspect of the transaction. To sustain it would result in giving to Equitable, which received the plaintiff's money and which was one of two parties ultimately to benefit by it, a status which would allow it to dissipate the money or appropriate it to its own purposes, and by so doing, at one and the same time prevent completion of the houses and destroy the plaintiff's right to realize upon its security. To state that proposition, it seems to me, is to answer it.

The defendant contends that the parol evidence rule forbids the Court to look through the paper screen and view the transaction as it really was. This, however, is not so. If the language is not free from doubt (and it is certainly not free from doubt in the present case) then the circumstances surrounding the making of the bond and particularly the purpose for which it was given, should be taken into account. Purdy v. Massey, 306 Pa. 288, 293. But even where language is plain and unambiguous, there are many situations in which circumstances may be resorted to to show that a transaction is, in reality, something entirely different from what it appears to be. For example, a clause expressly stipulating for liquidated damages may be shown to be a penalty. A transfer, absolute on its face, may be shown to have been given for security only. A document purporting to be a bailment lease will not prevent the Court from holding the transaction a conditional sale if such it was in fact.

In Purdy v. Massey, supra, the Court considered the entire transaction of which the bond was a part and, holding that the wording of the condition was not free from doubt, said, "In this case such considerations (the circumstances surrounding) lead to but one conclusion—that this bond was an absolute undertaking to . . . complete the building." That this statement was not dictum appears from the fact that the Supreme Court overruled two assign-

ments of error which squarely raised the point that the plaintiff, although she had shown failure to complete the building, had failed to show that it was by reason of default on the part of the principal.

So considered I find that the bond in this case was an absolute undertaking by the defendant directly to the plaintiff that the houses would be completed according to plans and specifications identified by reference to the operation agreement, that it was intended solely to secure the plaintiff's loan and was not intended to and did not guarantee full performance of the operation agreement, that it was not intended to and did not confer any rights (except contingently on full payment to the plaintiff) upon Equitable or its subsidiary, that the plaintiff was the real obligee and that no default on the part of the nominal obligees would affect the plaintiff's rights.

Therefore, it is wholly immaterial whether or not default on the part of Equitable or its subsidiary excused the builder from his obligation under the operation agreement. The plaintiff having acquired its right against the surety, not derivatively by assignment from Equitable but directly by virtue of its advances of money on the faith of the note, mortgages and bond, it is also immaterial that Equitable's subsidiary did not join in the assignment and its default (even if that could be considered its separate act) is no defense.

The third defense if supportable at all must be upon the theory that the surety bond was given solely as collateral security for the assigned mortgages. Again, I am unable to take the defendant's view of the transaction. The mortgages were pledges; the bond was collateral security in the broad sense of an obligation running alongside of the principal debt, according to the derivational meaning of the word "collateral." Both were given to secure the loan. On default, the bank had the right to look to all the collateral which it held or to any of it. Jennings v. Loeffler, 184 Pa. 318; Adelphia B. & L. Assn. v. Trilling, 121 Pa. Sup.

469; Stoflet v. Kress, 342 Pa. 332. The sale of the mortgages exhausted the plaintiff's rights against that particular group of collaterals and what happened to the mortgages thereafter, whether they were paid or released or satisfied, made no difference. But it did not carry the plaintiff's rights in the bond nor divest the plaintiff of its right to enforce the defendant's obligation to make good the loss. This result could have followed only if the bond had been given solely as collateral for the mortgages, and it would need evidence of a very different kind of transaction from that appearing here to compel that finding.

The argument that the renewal of the notes released the surety is fully met by the rule of Philadelphia to Use v. Fidelity and Deposit Co. of Maryland, 231 Pa. 208; Trustees of Methodist Episcopal Church of Franklin v. Equitable Surety Co., 269 Pa. 411, and other cases, holding that a paid surety will be relieved only if the extension or alteration in the terms of the contract is material and work to its disadvantage. There is nothing in the present case to show that the defendant incurred any detriment by reason of the notes having been renewed, and as a matter of fact, nothing to show that it suffered any loss by reason of the mortgages' sale, assignment and foreclosure.

In addition to the foregoing, the assertion of this (third) defense is plainly an attempt by the defendant to "mend its hold." "Where a party gives a reason for his conduct and decision touching anything in controversy, he is estopped, after litigation has begun, from changing his ground and putting his conduct upon another and different consideration," Railway Co. v. McCarthy, 96 U. S. 258. Even before formal notice of default, the defendant repudiated and denied all liability with respect to the bond and the one and only reason advanced to justify its position in so doing was its first defense, already considered. It reasserted this position ("in accordance with our former correspondence") after it had

been notified by the plaintiff of its intention to sell the mortgage collateral at auction and after it had been advised of such sales of the Furman and Roehm mortgages and the Storck bonds. As late as February 26, 1943 the defendant filed its affidavit of defense on the merits with new matter and made no suggestion of this third defense.

The fourth defense is without merit. The measure of damages is the cost of completion (Purdy v. Massey, supra; Leonard's Estate, 343 Pa. 198). There is evidence of the estimated cost of the entire operation, including an intemized breakdown of the estimated cost of the buildings. This latter, taken in connection with the stipulation as to what had actually been done when work stopped, furnishes satisfactory evidence of so much of the cost as is applicable to the partial performance, from which the balance or cost of completing the unfinished job can be ascertained by simple subtraction.

The fifth defense was fully considered on the defendant's motion to dismiss and the conclusion reached that the record as then presented failed to show any evidence of abandonment of its cause of action by the plaintiff and that the history of the proceeding did not require an involuntary dismissal for want of prosecution. Discovery procedure taken by the defendant in preparation for trial has not produced any additional support for its position. Whether it intends to press this defense any further, I do not know, but no request raising it has been presented.

The defendant objected to the entire testimony of the plaintiff's vice-president "for the reason that it is our position that the transaction between the Provident and the Equitable is not relevant to the issue before your court." Having held in the foregoing opinion that the transaction was relevant, I overrule the objection. Later in the witness' testimony various other objections were interposed none of which have any substantial merit and they are overruled. The rule against leading questions

has long ago been relaxed to permit the Court to exercise a sound discretion, in the interest of expediting the proceedings and clarifying the testimony where, in the Court's judgment, it can be done without danger of falsehood.

The plaintiff's vice-president testified that, without the bond, the loan would not have been made. While this testimony was properly received, I may say that it is a fact which I would find from the circumstances, entirely independently of the testimony.

Answers to Requests.

The stipulation of facts is adopted as the Court's special findings of fact. The view taken by the Court of the nature of the transaction involved in the case makes a number of facts stipulated immaterial and this also applies to a number of the defendant's requests. Such requests as are not covered by the facts as found above are held to be immaterial and are not answered. The statements of fact in the opinion may be taken as additional special findings, supplementing or modifying the facts as stipulated, and answering such requests as are not covered by the stipulation. The statements of law contained in the opinion may be taken as conclusions of law.

I affirm the plaintiff's requests for conclusions of law and deny the defendant's except the first which I affirm.

An order for judgment in accordance with the foregoing may be presented.

15272

Before (s) Kirkpatrick, *J.*

This action was upon the bond in the Storck operation which, in point of time, was the earliest of the three. The only difference between this action and No. 15270 is the fact that in the Storck transaction the builder's

application to the defendant for the surety bond contains the question and answer, "To whom to be given?" "Provident Trust Co., Trustee."—a fact which makes the defendant's knowledge of the real nature of the transaction even plainer than in the other case.

The facts and legal principles stated in the opinion in Action No. 15270 may be taken as special findings and conclusions in this one. In addition I affirm the plaintiff's requests for findings of fact and conclusions of law. It is unnecessary to answer such of the defendant's requests for findings of fact as are not covered by the foregoing, the reasons stated in No. 15270 being applicable. I deny all the defendant's requests for conclusions of law except the first, sixteenth and seventeenth, which are affirmed.

An order for judgment for the plaintiff may be presented.

OPINION

OF THE

UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

No. 15270.

Sur Motion for New Trial.

Before KIRKPATRICK, *J.*

This case turned mainly upon the scope of the defendant's obligation—whether the bond was for the faithful performance of the building contract or for the completion of the houses, regardless of reasons or excuses for their non-completion. The court found that it was the latter kind of bond.

In reaching its conclusions the court examined the entire transaction and found that the bond was intended to run directly to the plaintiff to secure its loan, the plaintiff being the real obligee, that the building operation had been

undertaken by, or through the medium of, Equitable Bonded Mortgage Company and that Equitable, although on paper an obligee, was in reality and to the knowledge of the plaintiff in the position of a principal along with the building contractor (the nominal principal). The defendant's chief contention in this motion for a new trial is that this view of the transaction was a pure figment of the court's imagination without anything in the record to warrant it.

Ample evidence supporting the court's findings is to be found in the stipulation, testimony, and exhibits, which fully disclose the circumstances surrounding the transaction, the manner in which it was consummated, the relationships of the various parties to it and their common knowledge of the objects to be attained.

However, it is also worth noting that the defendant itself is on record in the case with an explicit avowal that the real, as distinguished from the apparent, relationship of the parties was what the court found it to be. In the affidavit, filed in support of a motion to dismiss the action for want of prosecution and expressly incorporated in the written motion presented by the defendant's counsel, the following appears, "The said principals designated in the said bonds were in fact only straw parties acting on behalf of the said obligees which controlled the actions and operations of the said principals and such method of operation by the obligees was or should have been known to the plaintiff herein at the time of the assignment of the said bonds by the said obligees to plaintiff herein." It is also alleged that certain witnesses, if living, would have testified "that the said operations were actually the operations of the obligees (Equitable) designated in the said bonds, that the contractors in whose names the applications for the surety completion bonds were submitted, were actually dummy contractors working for and on behalf of the said obligees;" etc. The court did not go quite so far as to characterize the contractors as dummies, but, otherwise, the foregoing quotations epitomize

the court's view of Equitable's position in the transaction, and could have been adopted, in hæc verba, as one of the findings.

Although the court did not have this affidavit in mind in making the findings, he might well have considered it, under general principles relating to judicial notice. See U. S. v. City of Philadelphia, C. C. A. (3), 140 F. 2d 406; Perlman v. 322 West Seventy-Second Street Co., Inc., 127 F. 2d 716. The motion was more than a mere procedural step. Upon the facts asserted in it the defendant sought to persuade the court to dismiss the whole cause. In view of what appears in it, it is pretty hard to see much force in the argument which the defendant now makes that the view which the court took was wholly unwarranted, unexpected and prejudicial.

None of the other reasons presented in support of the motion has enough substantial merit to call for the granting of a new trial.

The motion is denied.

Sur Motion to Amend Findings.

The court did not intend to disurb or modify the stipulated facts in any particular, and the findings appearing in the opinion do not have that effect. In order to avoid any misunderstanding which the defendant may have upon the point, the opinion is amended by striking out the word "stipulated" in the third line of the last page and substituting the words "separately found." One or two other minor changes in the opinion heretofore made by the court are confirmed. The court amends its affirmance of the plaintiff's second request for conclusions of law by allowing interest at 3 percent instead of 6 percent, in order to conform with the court's later memorandum sur motion for judgment.

Sur Motion to Amend Judgment.

The motion is denied.

UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 8846 and 8847 October Term, 1945

PROVIDENT TRUST COMPANY OF PHILADELPHIA, a Corporation of the Commonwealth of Pennsylvania

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK, a Corporation Existing Under the Laws of the State of New York,
Appellant

APPEALS FROM THE JUDGMENTS OF THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

Argued October 5, 1945
Before ALBERT LEE STEPHENS, MARIS and GOODRICH,
Circuit Judges.

OPINION OF THE COURT
(Filed December 17, 1945)

By GOODRICH, *Circuit Judge.*

This case arises on appeal from two District Court judgments,[1] against a surety on three completion bonds in the aggregate amount of $868,264.79. Both cases are factually alike and present identical questions of law.[2] The persons involved are: Provident Trust Company of Philadelphia, plaintiff; Metropolitan Casualty Insurance Company of New York, defendant; and Equitable Bonded Indemnity Company with its wholly owned subsidiary, Equitable Securities Corporation. From the business operations of the Equitable companies with certain builders, Furman, Roehm and Storck, and their surety, the defendant Metropolitan, on the one hand, and the plaintiff Provident on the other, the present conflict of interests arose.

The case is in Federal Court on diversity grounds only. All the operative facts seem to have had their setting in Pennsylvania. Under the now well understood and established rule, Pennsylvania law is to be applied and Pennsylvania decisions, so far as found to be applicable to the questions in the case are controlling.[3]

The defendant's principal and most important point, while presented with considerable elaboration, brings the case down to a simple set of facts which, in turn, is controlled by simple and well settled propositions of law. The substance of the case on the defendant's theory is this: A builder undertakes certain operations. In the

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[1] One judgment was for $457,012.31 representing the full amount of two unpaid loans less a credit of $300 plus 3% interest for a little over 15 years; the other judgment was for $411,252.48 representing the full amount of Debenture Bonds, less a credit of $200 plus 3% interest for more than 15 years.

[2] The purely nominal difference is that in one case, plaintiff sues in an individual capacity on two of the bonds, and in the other case, it sues as trustee on the remaining bond.

[3] The decision referred to by appellee as presenting a case (Baglin v. Title Guaranty Surety Co., 166 Fed. 356, affirmed, 178 Fed. 682 (C.C.A. 3, 1909)) "so nearly identical" was decided long before Erie R. Co. v. Tompkins was ever dreamed of. A Federal Court decision upon a question of state law settled upon principles of "general commercial law" is no precedent now.

language of suretyship, he is the principal debtor. He is to be supplied with money by a creditor, in this instance Equitable. A completion bond is given by the defendant surety. With the consent of the principal debtor and surety, rights of the creditor (Equitable) are assigned to plaintiff Provident Trust Company. The principal debtor's project is never completed because the creditor (Equitable) fails to advance the funds promised. This failure excuses the debtor from its performance.[4] Since the principal debtor is not in default upon his performance, his surety is likewise not in default. Therefore the creditor (Equitable) cannot recover against the surety.[5] Provident is but the assignee of the creditor and the rights of the assignee rise no higher than the assignor.[6] Judgment must, therefore, be for the defendant. If the defendant is right in its argument that the facts in the instant case are essentially those in the statement just made, it is perfectly clear that it is right in its legal conclusion. Indeed, the plaintiff would not claim to the contrary.

The plaintiff, however, claims and got the District

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[4] Restatement Contracts, § 274(1) "In promises for an agreed exchange, any material failure of performance by one party not justified by the conduct of the other discharges the latter's duty to give the agreed exchange even though his promise is not in terms conditional." Pennsylvania Annotations § 274(1), in accord, cites a great variety of cases.

[5] Restatement Security § 126 "Where there is a promise for an agreed exchange between creditor and principal and there is a material failure of performance by the creditor not justified by the conduct of the principal, the surety is not liable to the creditor unless the principal has elected to treat the failure only as a partial breach." Pennsylvania Annotations § 126, *"Accord:* Gunnis v. Weigley, 114 Pa. 191, 6 A. 465 (1886)". See also: McShain v. Indemnity Insurance Company of North America, 338 Pa. 113, 12 A. (2d) 59 (1940); Young v. American Bonding Company, 228 Pa. 373, 77 A. 623 (1910).

[6] Restatement Contracts § 167(1) "An assignee's right against the obligor is subject to all limitations of the obligee's right, to all absolute and temporary defenses thereto and to all set-offs and counterclaims of the obligor which would have been available against the obligee had there been no assignment, provided that such defenses and set offs are based on facts existing at the time of the assignment, or are based on facts arising thereafter prior to knowledge of the assignment by the obligor". Pennsylvania Annotations § 167(1) in accord, cites a number of cases.

Judge to go along with the claim, that it is not the assignee of a contract made by the defendant with Equitable but the contract is essentially one with the plaintiff itself. Its rights are not, therefore, derived by assignment from Equitable, but are obligations running directly from defendant to plaintiff. Of course, if this is the substance of the transaction, the view set out above has no application. There were no conflicts of testimony to be resolved at the trial. Most of the facts were stipulated and the testimony of the one witness, A. G. Scattergood, Vice-President of the plaintiff, was not disputed but relied on by the defendant. Our question becomes, therefore, what is the legal conclusion to be drawn from facts rather than what are the facts themselves.

Are the plaintiff's rights based on an obligation running directly to it or do they arise only by assignment from Equitable? Plaintiff contends,[7] and the District Court agreed, that Provident was a direct obligee. The facts upon which this conclusion is based are these: the surety knew that Provident and not Equitable was to be the ultimate recipient of the bonds;[8] the bonds, assignment and consent to assignment were bound together as though they were a single document;[9] the whole transaction was consummated in a single day (except for advances of money) so that Equitable was only a fleeting holder of the instruments which were immediately transferred to Provident; the assignment was executed and consented to even before the bonds were

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[7] Plaintiff's theory is that the "primary purpose of the surety bonds was to protect Provident" and "the 'assignment' in the bonds was an 'assignment' in name only".

[8] The District Court points out that "* * * in the Storck transaction the builder's application to the defendant for the surety bond contains the question and answer, 'To whom to be given?' 'Provident Trust Co., Trustee'—a fact which makes the defendant's knowledge of the real nature of the transaction even plainer than in the other case." The Court adds, "The plaintiff's vice president testified that, without the bond, the loan would not have been made."

[9] The single document view rests on this in the District Court's own wording: "The bond and assignment, with a statement of the defendant's financial condition and a power of attorney authorizing the execution of the bond, were bound together and backed by a single office backer of the defendant."

delivered to Equitable;[10] and finally defendant's statement that the principals were straw men.[11] This we think is a fair summary of the points relied upon by plaintiff and sustained by the District Court to show an obligation direct to plaintiff.

But since we are here dealing with obligations arising out of words used by the parties, we had better give attention to the language they used, unless we are to put the cart before the horse. If that language is ambiguous, we may, of course, go behind it and examine the cartload of surrounding facts to try to find out what was meant. As might well be expected of large financial organizations skilled in their calling, and advised by able counsel, the language is clear and to the point. It is plainly the language of assignment. The bonds refer to Equitable and its subsidiary as "obligees". The assignments say that Equitable does "grant, bargain, sell, transfer, assign and set over" to Provident. They speak of the bond "so assigned" and of "this assignment" to Provident. They provide that if the mortgages be reassigned to Equitable, Provident will also "re-assign" its rights under the bond. Metropolitan and the builders state, "We hereby consent to the above assignment." The pleadings by Provident

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[10] This does not amount to a technical flaw in the assignment, however. For while the assignments and consents were executed before the bonds were delivered to Equitable, that delivery nonetheless preceded delivery of the assignments to Provident. Thus when the documents were handed to Equitable the bonds became effective by delivery and when "thereafter" as is stipulated, the documents were handed to Provident the assignment became effective by delivery. And in any event, even if the assignment had become effective before the bonds were delivered, the latter would still have been assignable as future interests. East Lewisburg Lumber & Mfg. Co. v. Marsh, 91 Pa. 96 (1879); Ruple v. Bindley, 91 Pa. 296 (1879); Citizens Trust & Surety Co. v. Howell, 19 Pa. Super. 255 (1902).

[11] The District Court states, "In the affidavit, filed in support of a motion to dismiss the action for want of prosecution and expressly incorporated in the written motion presented by the defendant's counsel, the following appears, 'The said principals designated in the said bonds were in fact only straw parties acting on behalf of the said obligee which controlled the actions and operations of the said principals and such method of operation by the obligees was or should have been known to the plaintiff herein at the time of the assignment of the said bonds by the said obligees to the plaintiff herein'."

speak of defendant surety having "executed its written consent to a certain written assignment" to plaintiff. It is further expressly stipulated that Metropolitan as surety and the builders as principals, "executed their written consent to a certain written assignment to Provident." And the plaintiff sues as assignee of a contract, not one praying for reformation of an instrument. This is clear, exact, accurate. Neither we nor Judge Learned Hand's twenty bishops could change its plain meaning.[12] We have no case of mistake here, nor reliance by one party on the superior skill or knowledge of the other, no dominant bargaining agency which has imposed its will on a weaker party by hiding the real nature of the transaction through language formed to its own advantage,[13] nor any other possible reason for disregarding a simple meaning clearly expressed.

Furthermore, we do not see that the various facts urged by the plaintiff to show that Provident was a direct

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[12] Judge Learned Hand in Hotchkiss v. National City Bank of New York, 200 Fed. 287, affirmed 231 U. S. 50 (1913): "A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent. If, however, it were proved by twenty bishops that either party when he used the words, intended something else than the usual meaning which the law imposes upon them, he would still be held, unless there was some mutual mistake, or something else of the sort."

[13] The District Court states, "But even where language is plain and unambiguous, there are many situations in which circumstances may be resorted to to show that a transaction is, in reality, something entirely different from what it appears to be." It cites as examples that a clause for "liquidated damages may be shown to be a penalty"; a "transfer, absolute on its face, may be shown to have been given for security only"; and a purported bailment lease shown to be a conditional sale. In all these instances courts cut through the transaction as the parties have written it. The purpose of forbidding a clog upon the equity of redemption is of course to protect a debtor against a dominant creditor. In the liquidated damage case there is the same element of public policy present plus the point that when parties are allowed to stipulate for damages at all they are, to some extent, substituting their own rules for those of the law. Obviously this is a privilege to be kept within limits. All these exceptions are inapplicable here, for this is but an ordinary bargain between strong and well advised business concerns. So long as they stay within the law they may deal as they please and neither needs the guardianship of a court.

obligee prove the conclusion. It was quite probable that Provident considered itself sufficiently protected as an assignee. The testimony of its vice president showed the company sometimes took obligations running directly to it. We have no doubt that in fact its officers knew the difference. We think the binding of all papers together is not a legally significant fact nor is the length of time Equitable held them before handing them over to Provident. The matter of the affidavit referred to above does not come within what has been said. It should be noted however that this was filed at an early stage in the proceedings among matters "intended to be proved" by defendant. It was before the answer and before the stipulations the parties entered into. We think it has no significance. Further, except for mutual mistake and reformation, the rule that contracts mean what they clearly say applies to both contracting parties.

There is one more problem which requires consideration. The plaintiff claims that the surety's obligation was an absolute one. It points out that the language of the condition of the bond is that "The buildings hereinbefore mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to." This, it says, is an absolute and unconditional promise to see that completion is accomplished. In Purdy v. Massey, 306 Pa. 288 (1932) the Supreme Court of Pennsylvania was discussing language in a completion bond and its problem was whether the language used by the surety constituted the promisor a guarantor or whether the promise was merely to indemnify. The court concluded that the language was an affirmative covenant to "complete the building in the event of default by the principal". It was found that there was default by the principal and the surety was held. But the court was not holding the surety as anything more than a guarantor of performance by the principal debtor.

Of course, it is possible for a surety to contract that

a thing will happen or that a given result shall be produced. We think it likely that ordinarily surety bonds are not so given because the ordinary concept of suretyship is that of one person backing up the performance of another.[14] The question is whether this particular bond, in the language quoted, creates a promise on the part of the defendant regardless of the default of anyone else. The surety company relies upon the Pennsylvania decision of Young v. American Bonding Company, 228 Pa. 373, 77 A. 623 (1910). The plaintiff strenuously urges that this case is not in point and the District Court was led to agree with it.[15] If the Young case is in point we think it establishes the proposition that the words used in this type of bond which, in turn, contains a reference to a contract, makes performance of the surety's promise conditioned upon the non-performance of the main contract by the principal debtor. If this case is in point it obviously governs us because, as stated above, the instant case is to be settled in accordance with Pennsylvania law. We quite realize that it is part of a mature system of law to make distinctions. Only an exceedingly primitive legal culture is unable, for instance, to distinguish between intentional killing and death through accident. But it is not part of a mature system of law to make distinctions without differences. We cannot see, upon this point, any difference between the American Bonding case and this one. We think the former decision controls. The conclusion of that control is that the defendant's liability was conditioned upon a default by the principal obligor, that is the builder. The builder was not in default because

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14 See Restatement Security § 82 and Comment thereto.

15 The District Court says it does not think the Young case rules because: "The difference in the wording of the conditions of the two bonds may be noted. It is slight but not entirely without signfiicance. In the Young case the condition was, 'if the said principals shall well and faithfully construct and complete . . .'. In the present case the condition is, 'That if the buildings hereinabove mentioned shall be fully constructed and completed . . .'." The Court goes on to point out that the subsidiary facts of the Young case and the instant case are also "fundamentally entirely different".

he had an excuse for non-performance. Neither is the surety.

This analysis of the case makes it unnecessary for us to consider the other arguments made by the defendant.

The judgments of the District Court are reversed.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945. No. 816

PROVIDENT TRUST COMPANY OF PHILADELPHIA, TRUSTEE,
Petitioner,

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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IN THE
Supreme Court of the United States

OCTOBER TERM, 1945. No. .

Provident Trust Company of Philadelphia, Trustee,

Petitioner,

v.

The Metropolitan Casualty Insurance Company of New York,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

TO THE HONORABLE, THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioner, a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, respectfully prays this Court for the issuance of a Writ of Certiorari to the Circuit Court of Appeals for the Third Circuit, to review the final judgment of that Court entered on December 17, 1945, reversing the judgment of the District Court of the United States for the Eastern District of Pennsylvania entered on July 24, 1944.

A certified transcript of the record in this case, including the proceedings in said Circuit Court of Appeals, together with the requisite additional copies thereof, is furnished herewith, in conformity with Rule 38 of this Court.

STATEMENT OF THE MATTER INVOLVED.

This case and its companion case (No. 8846 in the Circuit Court of Appeals) were tried together by the District Court and they present identical questions for decision here. The only difference is that in this case the plaintiff is suing as trustee and not in its individual capacity, as it does in the companion case.

The plaintiff is a Pennsylvania corporation and the defendant is a New York corporation. The amount involved is more than $3,000.00 and the jurisdiction of the Federal Courts is based upon the diversity of citizenship.

Judgment was for the plaintiff, now petitioner, in the District Court for the sum of $411,252.48 (R., p. 355a). This judgment was reversed by the Circuit Court of Appeals for the Third Circuit. Since neither the opinions of the District Court nor the Circuit Court of Appeals have been officially reported as yet, they are attached hereto in appendix form for the convenience of this Court.

The action is against a corporate surety, Respondent, on a bond, of the type known commonly as a "completion bond", given in connection with a building operation.

The District Court made findings of fact which were based upon stipulations of counsel and the testimony of one witness (R., pp. 48a-69a, 104a-167a, 347a, 364a). These findings are the basis of the following discussion.

The transaction giving rise to this suit was a building operation in 1928. The promoter of the operation, Equitable Bonded Mortgage Company (hereafter sometimes called "promoter" or "Equitable") entered into a written contract with a certain builder to advance money for the operation in return for mortgages on dwellings to be erected. The first mortgages were to go to Equitable and the second mortgages to Equitable's wholly owned subsidiary, Equitable Securities Corporation (R., pp. 55a,

219a, 337a, 326a, 342a). Equitable applied to petitioner trust company for a loan to obtain a substantial part of the necessary funds, the loan to be secured by the first mortgages covering the dwellings to be erected (R., p. 140a). The petitioner made an appraisal of the proposed buildings on a completed basis, and approved the loan subject to securing a surety bond to guarantee completion (R., pp. 140a-141a, 135a).

Petitioner thereupon became trustee under a trust agreement with Equitable to secure an authorized issue of Equitable's 5½% Gold Bonds, the trust estate to consist of the first mortgages and the surety completion bond (R., pp. 105a-106a).

The required bond was executed by respondent surety and builder on September 11, 1928 (R., p. 105a). Equitable was named therein as obligee, but Equitable simultaneously executed a written assignment to petitioner trust company, and even prior to delivery of the bond to Equitable the respondent surety executed its formal consent to the assignment. The bond, assignment, consent to assignment, power of attorney and statement of surety's financial condition were all bound together by surety and delivered to Equitable (R., pp. 105a, 413a). On September 13, 1928, Equitable delivered the document to petitioner along with the mortgages (R., p. 105a).

The condition of the bond was as follows:[1]

> "NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION IS SUCH, That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to, and herein incorporated with like force and effect as if attached hereto, free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation

[1] A photostatic copy of the bond and attached papers appears in the record at page 413a.

to be void; or else to be and remain in full force and effect."

On September 14, 1928, petitioner delivered $280,000 face value of Equitable's 5½% Gold Bonds to The Philadelphia National Bank as collateral security for a loan of $224,000 made by said Bank to Equitable (R., p. 106a). The said Gold Bonds became due on September 1, 1929, but they have never been paid (R., p. 106a). None of the buildings in the development was ever completed; and, in fact, most of them never proceeded beyond the cellar stage (R., p. 107a).

The respondent surety raised several defenses in the actions on the bonds but the only one of significance here, in view of the decision of the Circuit Court of Appeals, is that based upon the fact that Equitable had breached the building agreement by failing to make the total required advances to the builder.

The District Court entered judgment for petitioner in the total amount, including interest at 3%, of $411,252.48 on July 24, 1944. Its decision was based on its finding of fact that the parties had intended that the bond should be a direct obligation from the builder and respondent surety to petitioner, and that, hence, a breach of the agreement between the builder and Equitable was immaterial.

The Circuit Court of Appeals reversed this judgment on December 17, 1945. It gave two reasons for so doing. First was its finding of fact, contrary to the District Court's, that the parties had intended only that the petitioner should take the bond by assignment, and thus the surety could raise the defense of non-performance under the builder's agreement since it could have done so in an action by Equitable, petitioner's assignor. Secondly, the Circuit Court held that under the law of Pennsylvania a bond such as this is not given for the completion of the buildings but for the performance of the building contract.

BASIS OF THIS COURT'S JURISDICTION.

This Court has jurisdiction of this case under Section 240(a) of the Judicial Code of 1911, as amended by the Act of February 13, 1925, Chap. 229, Sect. 1; 28 U. S. C. A. Sect. 347. The opinion and final judgment of the Circuit Court of Appeals were entered December 17, 1945.

QUESTIONS PRESENTED.

1. Where a surety company (respondent) executes its bond for the construction of dwellings, which bond it knew would be used as security to obtain funds for construction from a lender (petitioner), and formally consents to the assignment of that bond by the nominal obligee to the lender prior to delivery of the bond to the nominal obligee, and the District Court finds from the evidence the fact that the parties intended that the obligation should be a direct one from the surety to the lender, may the Circuit Court of Appeals overrule or disregard that finding? (Brief, *infra*, pp. 11-19).

2. Under the law of Pennsylvania is a bond conditioned on the construction of specified buildings one guaranteeing the construction of those buildings or one guaranteeing the performance of the building agreement when reference to that agreement appears only in the recital and not in the condition of the bond? (Brief, *infra*, pp. 19-27).

3. May a Circuit Court of Appeals disregard the important rule of law applied in Pennsylvania that contracts of paid sureties shall be construed strictly against them? (Brief, *infra*, pp. 27-31).

4. May a Circuit Court of Appeals apply two different standards of interpretation of written instruments in same case to the consistent benefit of a paid surety and the consistent detriment of an innocent assured? (Brief, pp. 31-33).

REASONS RELIED UPON FOR GRANTING THE WRIT.

The discretionary power of this Court to grant a Writ of Certiorari is invoked upon the following grounds:

1. The Circuit Court of Appeals for the Third Circuit has departed so far from the accepted and usual course of judicial procedure, based upon Rule 52(a) of the Federal Rules of Civil Procedure and decisions of this Court, in overruling a District Court's finding of fact as to which there is substantial evidence, that this Court should exercise its supervisory powers.

2. The Circuit Court of Appeals for the Third Circuit has decided important questions of Pennsylvania law as to the proper interpretation of surety bonds in conflict with applicable Pennsylvania decisions.

3. The Circuit Court of Appeals for the Third Circuit has departed so far from the accepted and usual course of judicial proceedings by applying inconsistently two different standards of interpretation to the contracts involved in this case that this Court should exercise its supervisory powers.

WHEREFORE, your petitioner respectfully prays that a Writ of Certiorari be issued under the Seal of this Court, directed to the United States Circuit Court of Appeals for the Third Circuit, commanding said Court to certify and send to this Court on a day to be designated, a full and complete transcript of the record and all proceedings

of said Circuit Court of Appeals had in this cause, to the end that this cause may be reviewed and determined by this Court; that the judgment of said Circuit Court of Appeals be reversed; and that your petitioner be granted such other and further relief as to this Honorable Court may seem meet.

PROVIDENT TRUST COMPANY OF PHILADELPHIA,

By

WM. CLARKE MASON,
Counsel for Petitioner.

PHILADELPHIA,
February 5, 1946.

BRIEF APPLICABLE TO THIS AND COMPANION CASE IN SUPPORT OF BOTH PETITIONS.

I. OPINIONS OF THE COURTS BELOW.

The opinions of the District Court appear in the Record at pages 337a, 349a and 362a. They have not yet been officially reported. The opinion of the Circuit Court of Appeals, a part of the Record, has not yet been officially reported.

The opinions of both Courts are attached hereto in appendix form for the convenience of this Court.

II. JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code of 1911, as amended by the Act of February 13, 1925, Chap. 229, Sect. 1, 43 Stat. 936, 28 U. S. C. A., Sect. 347.

The judgment of the United States Circuit Court of Appeals for the Third Circuit, which Petitioner seeks to have reviewed, was filed on December 17, 1945.

III. STATEMENT OF THE CASE.

The essential facts on which this application rests are stated in the foregoing Petition for Writ of Certiorari. Insofar as may be required for a clear understanding of the several points of the ensuing argument, these facts will be supplemented by further references to the Record.

IV. SPECIFICATIONS OF ERROR.

The error which Petitioner intends to urge, if the Writ of Certiorari is granted, is that the Circuit Court of Appeals erred:

In failing to follow the finding of fact made by the District Court that the parties intended that the bond should run directly to Petitioner to secure its loans.

In holding, contrary to applicable decisions of the Supreme Court of Pennsylvania, that a bond given to secure the completion of buildings is conditioned upon the performance of the building agreement and not the construction of the buildings, even though the building agreement is referred to only in a recital.

In failing to follow the Pennsylvania rule that contracts of paid sureties will be construed strictly against them.

In failing to apply a consistent rule of interpretation as to the several agreements involved.

V. SUMMARY OF ARGUMENT.

1. The Circuit Court of Appeals disregarded the District Court's findings of fact which were supported by substantial evidence.

2. The construction placed upon the conditions of the bonds by the Circuit Court of Appeals is in conflict with applicable Pennsylvania decisions.

3. The rule, sustained by Pennsylvania decisions and decisions of this Court, that the contracts of paid sureties are to be construed strictly against them has not been followed by the Circuit Court of Appeals in these cases.

4. The decision of the Circuit Court of Appeals contains such a fundamental inconsistency that it constitutes a serious departure from the usual course of judicial procedure.

The Circuit Court of Appeals Disregarded the District Court's Findings of Fact Which Were Supported by Substantial Evidence.

The District Court adopted the stipulation of facts as part of its special findings of fact, and stated that "The statements of fact in the opinion may be taken as additional special findings, supplementing or modifying the facts as stipulated, and answering such requests as are not covered by the stipulation" (Appendix, p. 11a).

The District Court found as a fact from the circumstances involved that it was the intention of the parties that the bond was to run directly to the petitioner to secure its loan despite the fact that the transaction was in the form of a simultaneous assignment of the bond.

In its opinion, sur motion for new trial, the District Court summarized its original findings by making the following statement (Appendix, p. 12a).

> "In reaching its conclusions the court examined the entire transaction and *found that the bond was intended to run directly to the plaintiff to secure its loan,* the plaintiff being the real obligee, that the building operation had been undertaken by, or through the medium of, Equitable Bonded Mortgage Company and that Equitable, although on paper an obligee, was in reality and to the knowledge of the plaintiff in the position of a principal along with the building contractor (the nominal principal)." (Emphasis supplied.)

Under Rule 52(a) of the Federal Rules of Civil Procedure, it is stated that findings of fact shall not be set aside unless clearly erroneous.

Despite this clear injunction as to the effect to be given to findings of fact made by the trial court, the Circuit Court of Appeals for the Third Circuit saw fit to overrule the aforesaid finding of fact by the District Court

that the parties intended the petitioner to be a direct obligee. The Circuit Court of Appeals said (Appendix, p. 20a): "We do not see that the various facts urged by the Plaintiff to show that Provident was a direct obligee, prove the conclusion." At the time the Court made this statement the conclusion was an express finding of fact by the District Court and was no longer merely Petitioner's conclusion.

That there is ample evidence to support the District Court's finding as to the intention of the parties is apparent from the following evidentiary facts also found by the District Court and affirmed by the Circuit Court of Appeals (Appendix, pp. 18a-19a):

(1) The Respondent surety knew that the Petitioner and not the Equitable Bonded Mortgage Company was to be the ultimate recipient of the bonds.

(2) The assignment and consent to assignment, by Respondent surety, were executed before the bonds were even delivered to the nominal obligee, Equitable Bonded Mortgage Company, by Respondent surety.

(3) In each case the bond, assignment, consent to assignment, power of attorney authorizing the execution of the bond and a statement of Respondent's financial condition, were bound together as one instrument by Respondent surety prior to delivery to the nominal obligee, Equitable Bonded Mortgage Company.

(4) The whole transaction of delivery by Respondent surety to Equitable Bonded Mortgage Company and then to Petitioner was completed on the same day so that Equitable held the bonds only momentarily.

(5) The Petitioner required that construction bonds be furnished as collateral before it would loan its money to Equitable Bonded Mortgage Company.

In the light of these basic facts it is impossible to say that the ultimate finding of the District Court was "clearly erroneous"; and it is only on such a basis that the Circuit Court of Appeals had the power to disregard it.

Prior to the adoption of Rule 52 (a) this Court had already held that an appellate court cannot review the evidence for the purpose of drawing its own inference or conclusion therefrom at variance with the trial judge's finding of fact. Thus, in *McCaughn* v. *Real Estate L. T. & T. Co.*, 297 U. S. 606, this Court reversed the judgment of the Circuit Court of Appeals for the Third Circuit on the sole ground that the Circuit Court had failed to follow the District Court's finding that a gift had been made in contemplation of death. It was there said (p. 608):

> "The instant case is controlled by the established rules relating to appellate review in actions at law where a jury trial has been waived. R. S. 649, 700; 28 U. S. C. 773, 875. Where a general verdict is found by the trial court, it has the same effect as the verdict of a jury. The appellate court cannot pass upon the weight of evidence. * * * The ultimate question for the decision of the trial court was one of fact and its general verdict was conclusive. The Circuit Court of Appeals was without authority to weigh the evidence and to make its own findings."

This decision was recently cited with approval by this Court in *Allen* v. *Trust Company of Georgia, et al*, October Term, No. 289, decided January 28, 1946.

In *Tennessee Coal Company* v. *Muscoda Local*, 321 U. S. 590, decided subsequent to the adoption of Rule 52 (a), this Court recently considered the binding effect of the District Court's finding of fact with respect to the alleged existence of a custom in the coal mining business for the payment of wages during underground travel. It was there said by Mr. Justice Murphy (page 602):

> "We thus cannot say that the District Court's findings as to custom and contract are so clearly erroneous as to compel us to disregard them."

In *Commissioner of Internal Revenue* v. *Scottish American Investment Company, Ltd.*, 323 U. S. 119, this

Court, speaking again through Mr. Justice Murphy, made the following statement, which is particularly pertinent in the instant cases (page 124):

> "The Circuit Courts of Appeal have no power to change or add to those findings of fact or to reweigh the evidence. And when the Tax Court's factual inferences and conclusions are determinative of compliance with statutory requirements, the appellate courts are limited to a determination of whether they have any substantial basis in the evidence. *The judicial eye must not in the first instance rove about searching for evidence to support other conflicting inferences and conclusions which the judges or the litigants may consider more reasonable or desirable.* It must be cast directly and primarily upon the evidence in support of those made by the Tax Court. If a substantial basis is lacking the appellate court may then indulge in making its own inferences and conclusions or it may remand the case to the Tax Court for further appropriate proceedings. But if such a basis is present the process of judicial review is at an end." (Emphasis supplied.)

In the instant cases the evidentiary facts were supplied by a stipulation and the testimony of one witness. As shown by the decision of this Court in the *Scottish American* case, *supra,* the conclusion of ultimate fact as to the intention of the parties by the District Court, is in itself a fact which cannot be disturbed unless clearly erroneous. The Circuit Court's misconception as to the conclusive nature of the District Court's findings based upon the undisputed evidentiary facts is apparent from the following statement in its opinion (App., p. 18a):

> "There were no conflicts of testimony to be resolved at the trial. Most of the facts were stipulated and the testimony of the one witness, A. G. Scattergood,

Vice-President of the plaintiff, was not disputed but relied on by the defendant. Our question becomes, therefore, what is the legal conclusion to be drawn from facts rather than what are the facts themselves."

It has been held by this Court that, insofar as the binding nature of the findings of fact are concerned, there is no difference between those which are based on stipulation and those which are based upon disputed testimony. Thus, in *Boehm* v. *Commissioner of Internal Revenue,* 90 L. ed. 96 (not yet reported officially), the following statement was made (p. 100):

> "The circumstance that the facts in a particular case may be stipulated or undisputed does not make this issue any less factual in nature. The Tax Court is entitled to draw whatever inferences and conclusions it deems reasonable from such facts. * * * If it is in accordance, [with law] it is immaterial that different inferences and conclusions might clearly be drawn from the undisputed facts."

The foregoing opinions by this Court in the *Scottish American* case and in the *Boehm* case were rendered in deciding appeals from the Tax Court. However, since in such cases the findings can be disregarded if they do not have "any substantial basis in the evidence", those decisions can be applied equally well under Rule 52 (a) where the finding is conclusive unless "clearly erroneous". In *National Mutual Casualty Co.* v. *Eisenhower,* 116 F. (2d) 891 (C. C. A. 10th, 1940) the Circuit Court of Appeals for the Tenth Circuit adopted the same reasoning under Rule 52 (a) as this Court applied in the *Scottish American* case. It was there said (p. 894):

> "Contradictions and conflicts of evidence are for the trier of the facts, whether it be court or jury, and where the evidence and the inferences fairly deducible

> from it are such that reasonable minds may honestly draw different conclusions from them, it has been held by this court that the question is not one of law, but of fact, to be determined by the trier of the facts."

It does not clearly appear from the opinion of the Circuit Court of Appeals whether that Court considered the question one of fact or of law. At one point, as has been seen, the Court treated the issue as a factual one, and at another point it considered only the wording of the assignments apart from the surrounding circumstances, thus implying a legal question solely. However, the Circuit Court of Appeals was not at liberty to nullify the effect of the Trial Court's finding by considering it in any light other than as a finding of fact.

It has long been held that the giving and execution of contemporaneous agreements, under circumstances which indicate that the parties intend to achieve a different result thereby than that apparent on the face of the instruments, makes the interpretation of the contemporaneous agreements a question of fact to be decided by the jury or by the judge, if sitting alone, as in this case.

The most revealing case on this subject is *Bogk* v. *Gassert,* 149 U. S. 17, decided by this Court in 1893. In that case two deeds, an agreement to reconvey, and a lease, all for the same land, were executed simultaneously by the parties. The suit was on the lease. The other contemporaneous agreements were put in evidence by the defendant along with other evidence as to the intention of the parties, asserting that the whole disclosed that the parties had intended a mortgage. This Court there said (page 29):

> "The case was evidently a proper one to go to the jury, who were left to determine the question whether the instruments were *intended* as a mortgage, and were instructed that, if they found them to be such, the plaintiffs could not recover." (Emphasis supplied.)

The foregoing rule also applies in Pennsylvania. Thus, in *Harper's Appeal,* 64 Pa. 315, it was held by the Pennsylvania Supreme Court that *the finding by the Trial Judge* that an absolute deed accompanied by a separate instrument, in which the grantee agreed to reconvey the property at the grantor's request within three years, was intended to have the effect of a mortgage, would not be disturbed on appeal without a conclusive showing to the contrary. It was there said (page 319):

> "Accepting the opinion of the court below as the report of a master upon the evidence, we see no plain mistake in the conclusion at which they arrived, that the agreement of March 19th 1858 was cotemporaneous with the deed of March 18th 1858, from Gubbings and wife to Harper. Without very clear and persuasive evidence that the sale was an absolute one, and the agreement to reconvey a subsequent, distinct and independent contract, we must treat the transaction as a mortgage. Such, undoubtedly, is the result of the authorities in this state: Colwell *v.* Woods, 3 Watts 188; Kerr *v.* Gillmore, 6 Id. 405; Jaques *v.* Weeks, 7 Id. 261; Brown *v.* Nickle, 6 Barr 390; Reitenbaugh *v.* Ludwick, 7 Casey 131; Wilson *v.* Shoenberger's ex'rs., Id. 295."

Likewise, in *Herman* v. *Pepper,* 311 Pa. 104, 166 Atl. 587, the Pennsylvania Supreme Court did not disturb *the finding of a Court of Equity* that an assignment of a partner's interest, absolute on its face but in fact given as security for a loan and accompanied by a separate agreement to reassign upon payment thereof, was in fact a pledge.

See also *Huston* v. *Regn,* 184 Pa. 419, 39 Atl. 208; and *McCollum* v. *Braddock Trust Company,* 330 Pa. 293, 198 Atl. 803.

The instant case is indistinguishable in principle from *Bogk* v. *Gassert, supra,* and the other cases cited above.[2] The bonds, assignments thereof and consents were executed contemporaneously. In fact, the assignments and consents were executed in advance of the time that the bonds became effective by delivery. Under such circumstances the intent of the parties was a fact to be determined by the trial court from all the circumstances, and, once having been determined, the Circuit Court of Appeals was not at liberty to set it aside unless clearly unsupported by evidence.

In *Biggs* v. *Mays,* 125 F. (2d) 693 (C. C. A. 8th, 1942), the Circuit Court of Appeals for the Eighth Circuit considered itself bound to follow Rule 52(a) in a case similar to the instant ones. In that case the question was whether the acts and words of a debtor constituted a promise to pay which had tolled the running of the Arkansas statute of limitations, a question of fact under the Arkansas law. The Court said (p. 699):

> "The court below found specifically that 'the facts do not justify any inference of a promise to pay the note as demanded by the claimant.' Under the law of Arkansas, as outlined above, the inference of a promise to pay *is one of fact,* and the finding of the court is binding unless clearly erroneous. Rule 52(a) of the Rules of Civil Procedure, 28 U. S. C. A. following section 723c."

In the instant case in arriving at its determination that the parties intended merely an ordinary assignment, the Circuit Court of Appeals for the Third Circuit ignored the following Federal Rules: (A) That an appellate court shall not draw its own conclusions and inferences from the evidence; (B) That findings based on

[2] The Circuit Court appears to have disregarded the principle of these cases in the mistaken belief that the decisions were based upon reliance upon superior skill, mistake or domination of one party by the other. That such is not the case is apparent from even a cursory reading of the opinions.

undisputed facts are as conclusive as those based on disputed ones; and (C) That a finding of fact shall not be set aside unless clearly erroneous.

Thus, we have here a situation in which the Circuit Court of Appeals has disregarded an express finding of fact by a District Court, supported by substantial evidence, which fact is not only relevant but is determinative of the issues involved in these cases. The writ should issue to correct this abuse of appellate review.

The Construction Placed Upon the Conditions of the Bonds by the Circuit Court of Appeals is in Conflict with Applicable Pennsylvania Decisions.

The Circuit Court of Appeals based its decision as to the proper interpretation to be placed upon the condition in the bond on the following statement of what it considers to be the law of Pennsylvania (Appendix, p. 22a):

> "If the Young case (Young *v.* American Bonding Company, 228 Pa. 373, 77 Atl. 623) is in point, we think it establishes the proposition that the words used in this type of bond which, in turn, contains a reference to a contract, makes performance of the surety's promise conditioned upon the non-performance of the main contract by the principal debtor."

Following this statement of its concept of the law of Pennsylvania, the Court held that the condition of the bond should be construed in the light of the terms of the contract mentioned in the recital. Hence the failure of the nominal obligee to perform under the contract constituted a defense for the surety.

This statement of the law is correct only if the reference to the contract appears in the *condition* of the bond. It is totally incorrect if the reference to the contract appears merely *in a recital* of the bond, as in these cases.

The recitals and the condition of each bond in the instant cases are as follows:[3]

> "WHEREAS, the Principal has entered into a written agreement dated the 15th day of October 1928, with the Equitable Bonded Mortgage Company for the erection and completion of twenty (20) dwellings on Southeast side of Wadsworth Avenue, between Anderson Street and Ardleigh Street, 22nd Ward, City of Philadelphia, in accordance with certain plans and specifications duly signed and approved by all parties interested; and
>
> "WHEREAS, the Equitable Bonded Mortgage Company has agreed to advance One Hundred Forty-two Thousand Dollars ($142,000.) for the purchase of, and to be secured by assignments of first mortgages on the above mentioned dwellings, and
>
> "WHEREAS, the Equitable Securities Corporation has agreed to advance Eighty-one Thousand Dollars ($81,000.00) for the purchase of, and to be secured by assignments of second mortgages on the above mentioned dwellings.
>
> "NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION IS SUCH, That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to, and herein incorporated with like force and effect as if attached hereto, free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect."

Certain things should be noted about this bond preliminarily. The first recital refers to two different things.

[3] The only differences between the bonds are the names of the builders, the amounts involved, and the location of the property.

The first is a contract between the builder and Equitable for the construction of the dwellings, and in which Equitable promised to pay the builder. The second is the plans and specifications according to which the houses were to be built. The condition is that the buildings shall be built—*not in accordance with the contract*, but—*in accordance with the plans and specifications*, which are expressly incorporated as if attached thereto.

It is, of course, obvious that the extent of the undertaking of the principal and surety in any bond is the condition of the bond. The prefacing of the condition by recitals is usually only for the purpose of setting forth the background for the condition.

In Pennsylvania the Courts look to the recitals of a bond to explain the condition thereof only in certain types of cases. Thus, if the condition is so indefinite as to be unenforceable, the Court will resort to recitals in order to clarify the condition: *United States* v. *Morrisdale Coal Co.*, 50 Fed. Supp. 138 (D. C. E. D., Pa., 1942); or if the basic contract, for the performance of which the bond is really given, is set forth in complete detail in a recital, the Court will interpret the condition in the light of the contract so set forth: *Nazareth F. & M. Co.* v. *Marshall Co.*, 258 Pa. 558, 102 Atl. 268.

It is readily apparent that the instant case does not fall within either of the foregoing categories. Thus, the recital merely mentions the existence of the builder's agreement and there is no attempt to set forth in detail any of the terms of that agreement. Nor can it be said by any stretch of the imagination that the condition of the bond is so indefinite as to need explanation or amplification by the recitals in the bond.

There is one last exception to the general rule that the condition of the bond alone measures the liability of the parties thereto. That exception is the one which the Circuit Court of Appeals in these cases has mistakenly applied as a general rule. There are two cases which

give rise to this exception. One is the *Young* case, cited by the Circuit Court, and the other is *Dunbar* v. *Fleisher,* 137 Pa. 85, 20 Atl. 520. To show the genesis of this exception, and thereby clarify the decision in the *Young* case, the holding of the Pennsylvania Supreme Court in *Dunbar* v. *Fleisher* will be considered first. In that case the defendant, Fleisher, was surety on a bond for the faithful performance by two men, Harper and Famous, of certain masonry work *"as per contract"* between those two men and the plaintiff.[4] The said Harper and Famous did not perform the masonry work and this action was against the defendant on his surety bond. The defense was that payments required to have been made to Harper and Famous by the plaintiff had not been made and that therefore the defendant was relieved of his obligation, the same defense which the defendant has raised in this case. It was there held by the Supreme Court of Pennsylvania, in affirming judgment for the defendant, that the defense of non-payment under the terms of the principal contract was properly raised since *the condition* of the bond expressly referred to that contract.

Young v. *American Bonding Company, supra,* is the same as the *Dunbar* case. In the *Young* case the bond in suit was also a construction bond. It recited the existence of the contract under which the construction improvements were to be made, and was conditioned upon the faithful completion of those improvements *"as provided in said agreement".*[5] The Supreme Court of Pennsyl-

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[4] "Whereas, J. R. Dunbar has this day given to Jesse Harper and John Famous an order on the county commissioners for $62, or the amount that shall be due them for mason work at the completion of the bridge in Penn township, Perry county, Pennsylvania. Now, in consideration of $1 to me in hand paid, I hereby become security for said Harper and Famous for the faithful performance of said mason work to said bridge, *as per contract* with said J. R. Dunbar." (Emphasis supplied.)

[5] "Now therefore the condition of this obligation is such that if the said principals shall well and faithfully construct and complete said improvements of the value of Three Hundred and Fifty Thousand Dollars ($350,000) upon said property, *as provided in said agreement,* on or before the 31st day of December, 1906, then this obligation to be null and void; otherwise it shall remain in full force and effect." (Emphasis supplied.)

vania again held, and properly so, that the undertaking of the surety, as shown by the condition of the bond, was subject to the terms of the agreement since the condition expressly referred to that agreement.

The reason behind the decisions in the *Young* case and the *Dunbar* case is plain. The condition of the bond was that certain things be done in accordance with a contract, and therefore the contract became a part of the condition. It is merely a specific application of an elementary rule of interpretation.

In the instant cases, unlike the *Young* case and the *Dunbar* case, however, *the condition* of the bond makes no reference to the agreement between the builder and the promoter. It is only in the recital that the contract appears at all. To hold, as the Circuit Court did in these cases, is to build one exception to the general rule on top of another exception, that is, to construe a clear condition needing no explanation in the light of a contract mentioned only in a recital and not even referred to in the condition.

The strained nature of this interpretation is particularly apparent from the fact the parties showed clearly that they knew how to incorporate by reference. The condition is that the houses shall be built by either the builder named in the bond or by the surety "in accordance with *the plans and specifications* above referred to, and herein incorporated with like force and effect as if attached hereto". By applying the common-sense rule of *expressio unius est exclusio alterius* it is evident that the parties intended that the contract should *not* be a part of the condition.

The decision of the Pennsylvania Supreme Court in the case of *Purdy* v. *Massey,* 306 Pa. 288, 159 Atl. 545, states the law clearly applicable here. Due to the fact that certain phases of that case are so similar to the ones in the instant case, it is felt that the following detailed

discussion is merited.[6] In that case the owner of land had entered into a written agreement with the builder for the construction of a garage in accordance with detailed plans and specifications. The plaintiff agreed to subordinate her first mortgage on the land to a new mortgage, the proceeds of which were to be used to finance the construction. In return for subordinating her first mortgage, the plaintiff asked for, and received, a surety bond which, after reciting the existence of the construction agreement between the builder and owner, contained the condition that provided the builder should "complete the buildings mentioned free and clear of mechanics' liens or claims, then this obligation shall be void; otherwise to be and remain in full force and effect". The garage was never built and this suit was upon the bond against the builder and the surety. After judgment for the plaintiff in the Trial Court, the defendant surety appealed, and one of its assignments of error was that the Trial Court had refused to charge that there was no default on the part of the builder since the builder had never received the money payments required by the contract, the same defense as in the present cases. This assignment of error was overruled by the Pennsylvania Supreme Court and the judgment of the Court below was affirmed. The Court held that the undertaking by the defendant surety was an absolute one for the construction of the garage, and that the terms of the contract did not enter into the interpretation of the bond condition. It said:

> "The covenants in a bond 'should be construed to mean what the parties intended in so far as that intention can be ascertained by the words used': Equitable Trust Co. *v.* National Surety Co., *supra.* If, however, the language is not free from doubt, then the circumstances surrounding the making of the bond, and particularly the purpose for which it was given,

[6] The information appearing in this discussion which does not also appear in the printed report of the case, was obtained from the original record.

should be taken into account: March *v.* Allabough, 103 Pa. 335; Ambridge *v.* P. & B. St. Ry. Co., 234 Pa. 157. In this case such considerations lead to but one conclusion—*that this bond was an absolute undertaking to erect and complete the building.*

"This bond is to be construed most strictly in favor of the plaintiff. The obligor, Indemnity Insurance Company of North America, is a paid surety engaged in the business of furnishing bonds for profit; we have frequently held that in cases of corporate sureties, the bond is to be strictly construed in favor of the obligee: Young *v.* American Bonding Co., 228 Pa. 373; South Philadelphia State Bank *v.* National Surety Co., 288 Pa. 300, and cases there cited.

"*The condition of the bond is performance of a specific thing—completion of the building provided for in plans and specifications made a part of the bond—and the only alternative for performance is the bond itself.* It is obvious, being clearly expressed by the words of the bond and the circumstances surrounding the transaction, that the intent of all concerned was to give plaintiff in lieu of her first mortgage the enhanced value of the real estate by the addition of the building, or failing that, its equivalent in money—not to exceed the face value of the bond." (Emphasis supplied.)

The decision in the *Purdy* case is clearly in point here. The recital mentioned the builder's contract, the condition did not, and the court held that the bond was an absolute undertaking that the structure be built. Furthermore, it can be said with equal force in this case that the purpose of the bond was to give Petitioner "the enhanced value of the real estate by the addition of the building, or failing that, its equivalent in money."

It will be noticed from the decision of the Court in the *Purdy* case that if the language of the bond is not free from doubt "then the circumstances surrounding the making of the bond, and particularly the purpose for which it was given, should be taken into account". The Petitioner believes that the language is clear and unambiguous, but since the Circuit Court of Appeals did not, or otherwise it would not have resorted to the contract, it should have followed the findings of fact by the District Court. That Court considered the case as one requiring an examination of the surrounding circumstances and found as follows (App., p. 8a):

> "So considered I find that the bond in this case was an absolute undertaking by the defendant directly to the plaintiff that the houses would be completed according to plans and specifications identified by reference to the operation agreement, that it was intended solely to secure the plaintiff's loan and was not intended to and did not guarantee full performance of the operation agreement, that it was not intended to and did not confer any rights (except contingently on full payment to the plaintiff) upon Equitable or its subsidiary, that the plaintiff was the real obligee and that no default on the part of the nominal obligees would affect the plaintiff's rights."

Since the Circuit Court of Appeals believed that the language was ambiguous, it was no more at liberty to disregard the District Court's finding in this particular than it was as to the parties' intent in making the "assignment" (see *supra*, pp. 13-16).

The discretionary power of this Court may be invoked to grant a writ of certiorari when a Circuit Court of Appeals has made an error in interpreting an important question of local law. The importance to the Petitioner of the error in these cases can be seen from the fact that

the judgments in these companion cases total almost a million dollars. The importance of the decision to those dealing with surety bonds in Pennsylvania can also be seen from the fact that the door has been opened now to interpretation in the light of any and all recitals unless it is expressly stated that they are *not* a part of the condition. If that is to be the law, when heretofore only the contrary was true, a great deal of the collateral held by financial institutions in Pennsylvania has decreased in value over night. This Court should exercise its power to review these cases and set at rest the doubts created by the Circuit Court of Appeals' decision.

The Rule, Sustained by Pennsylvania Decisions and Decisions of This Court, that the Contracts of Paid Sureties Are to Be Construed Strictly Against Them, Has Not Been Followed by the Circuit Court of Appeals in These Cases.

It is a settled rule in Pennsylvania, as it is throughout this country generally, that the contract of a paid surety will be construed most strongly against the surety and that all doubts and technicalities arising in said undertakings will be resolved in favor of the obligee. A typical statement of this rule appears in *Mechanics Trust Co.* v. *Fidelity & Casualty Co.*, 304 Pa. 526, 156 Atl. 146, where it was said (p. 533):

> "We have frequently said that the trend of modern decisions, federal and state, has been to distinguish between individual and corporate suretyship, where the surety has undertaken, for money, the contract of suretyship which it is its business to sell; in such cases, the contract should be construed most strictly in favor of the obligee: South Philadelphia State Bank *v.* National Surety Co., 288 Pa. 300, 305-6, and cases there cited."

See also, *Monongahela Street Railway* v. *Philadelphia Co.,* 350 Pa. 603, 617, 39 A. (2nd) 909; *Fiumara* v. *American Surety Co.,* 346 Pa. 584, 595, 31 A. (2nd) 283; *Hess* v. *Merion Title & Trust Co.,* 317 Pa. 501, 505, 177 Atl. 53; *Sokoloff* v. *Fidelity & Casualty Co. of N. Y.,* 288 Pa. 211, 215, 135 Atl. 746.

In spite of this well established rule of construction, the Circuit Court of Appeals construed the bonds in suit in favor of the paid surety. In fact, it may well be said that the Court treated the Respondent as though it were a volunteer surety, a favorite of the law.

The Petitioner does not believe that the language of the bond need be strained to be construed against the Respondent Surety in order to hold that the condition of the bond is absolute for the building of the houses. It is submitted that the mere reading of the bond itself, without construing it expressly in favor of one party or the other, leads inevitably to that conclusion. On the other hand, however, the Petitioner is aggrieved by the obvious fact that the condition of the bond was construed against it, an assured, and in favor of the Respondent, a paid surety.

It was the business of the Respondent to insure the undertakings of other persons. It is experienced and, presumably, normally efficient in this business. If the Respondent had intended originally that its obligation to construct the dwellings should be dependent upon the performance of the building contract between the builder and the promoter, it could have protected itself by inserting a reference to that contract in the condition of the bond, or by merely guaranteeing the performance of that contract. The surety disclosed in the condition as written the fact that it knew how to incorporate extraneous documents into the condition of the bond, for it did so as to the plans and specifications for the dwellings which, like the contract, were referred to in the recital. In the face of this demonstration of skill in draftsmanship, one must

be most solicitous of the welfare of the surety to conclude that the contract was also incorporated in the condition.

Only by distorting the language of the instrument is one able to reach the conclusion, achieved without apparent difficulty by the Circuit Court of Appeals, that the Respondent Surety had premised the performance of its undertaking upon the accomplishment by the promoter of all the many acts required of it in its contract with the builder. If clear and unambiguous language is to be perverted by "interpretation", let that be done for the benefit of the innocent lender, and not for the gain of the paid surety.

The ultimate effect of favoring the surety in this instance is stated by the District Court (App., p. 7a):

> "To sustain it (the Respondent's contention) would result in giving to Equitable, which received the plaintiff's money and which was one of two parties ultimately to benefit by it, a status which would allow it to dissipate the money or appropriate it to its own purposes, and by doing so, at one and the same time prevent completion of the houses and destroy the plaintiff's right to realize upon its security. To state that proposition, it seems to me, is to answer it."

The Circuit Court of Appeals, by its decision in this case, manifestly has accorded to Respondent Surety a position completely at variance with the one to which it is entitled under the general rule. The Court has therefore misapplied, and not merely failed to apply, an important rule of Pennsylvania law.

The principle that contracts of paid sureties will be construed against them was called to the attention of the Circuit Court of Appeals by counsel for Petitioner by citing the case of *Baglin* v. *Title Guaranty & Surety Co.*, 166 Fed. 356; affirmed 178 Fed. 682 (C. C. A. 3rd, 1909). This authority was summarily disposed of by the Circuit

Court of Appeals in the following footnote to its opinion (App., p. 16a):

> "The decision referred to by appellee as presenting a case (Baglin *v.* Title Guaranty Surety Co., 166 Fed. 356, affirmed 178 Fed. 682 (C. C. A. 3, 1909)) 'so nearly identical' was decided long before Erie R. Co. *v.* Tompkins was ever dreamed of. A Federal Court decision upon a question of state law settled upon principles of 'general commercial law' is no precedent now."

A careful reading of the opinions in the *Baglin* case would clearly show that these opinions state not only the general law applicable to the defense of a paid surety, but record the then and present law of Pennsylvania—all contrary to the different and new law now made by the decision of the Circuit Court of Appeals herein complained of. The following quotations from the *Baglin* case show how erroneous the footnote is:

By Judge McPherson (166 Fed. 363):

> "Nor is there any reason to be astute in looking about for flaws that may invalidate the transaction. The defendant is not entitled to the tender consideration that is accorded to an individual surety who is a mere volunteer. Surety companies are not to be so described; they are insurers, paid for their services, bound by contracts which are usually carefully drawn by themselves, and, as a general rule, satisfactorily secured by counter indemnity. They perform a most useful, and indeed, according to modern custom, an indispensable, function in the business and legal world, but they differ so much from an individual surety of the ordinary type as to render inapplicable some of the reasons that have led the courts to guard the rights of the individual surety with jealous care."

By the Circuit Court of Appeals, affirming (178 Fed. 687):

> "• • • The bond sued upon is not an indemnity bond. Defendant is bound, as surety or guarantor, to the plaintiff, as obligee in the bond, and, in the words of the trial judge, 'the fact remains that the guarantee in question was given and paid for; that it warranted the performance of a lawful act, and that such act has not been performed,' and by its nonperformance, defendant's liability is fixed."

Petitioner respectfully submits that if a new rule of law is to be established now by judicial fiat, to relieve a paid surety from its contract obligations, it should be established by a decision of this Court, after full consideration, and not by the Circuit Court of Appeals for the Third Circuit.

The Decision of the Circuit Court of Appeals Contains Such a Fundamental Inconsistency That it Constitutes a Serious Departure From the Usual Course of Judicial Procedure.

As has been seen, the Circuit Court of Appeals judged this case from two aspects. First, it considered whether the transaction was an assignment of the bond which would permit the Respondent Surety to raise a defense against the Petitioner which it would have had against the nominal obligee, or whether it was a direct obligation to Petitioner. Secondly, it considered whether the bond was an absolute undertaking, or whether the condition of the bond was itself conditioned upon the performance of the building contract. In the first instance, the Court held that the transaction was an ordinary assignment; and, in the second instance, it determined that the condition of the bond was modified by the terms of the building contract.

In deciding that the Petitioner was merely an assignee of the bond, the Court said that the language used in the instrument was not ambiguous and that therefore it would not consider the surrounding circumstances in determining the intent of the parties. However, in construing the condition of the bond, the language of which is certainly as clear and definite as that of the assignment, the Court read into it the terms of the main contract between the nominal Obligee and the Obligor Builder, which contract was not even referred to in the condition.

Despite the fact that the Circuit Court of Appeals stated in its opinion that "the rule that contracts mean what they clearly say applies to both contracting parties", the Court nevertheless applied a rule of strict construction to the benefit of the paid surety in one phase of the case; and, in the other phase of the case, in which the rule of strict construction should have been applied, it chose to adopt a liberal and strained construction, also to the benefit of Respondent Surety.

If the Circuit Court of Appeals had consistently applied the first rule which it employed, namely, that only the exact language of the contract will be considered, it would necessarily have had to find that the condition of the bond was absolute for the construction of the dwellings in any event. Nothing could be more certain or unambiguous than the covenant in the bond that "if the buildings hereinabove mentioned shall be fully constructed and completed * * * free and clear of mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect".

On the other hand, if it had applied throughout the second rule which it adopted, namely, that matters extraneous to the agreement may be considered in interpretation, it would have followed the finding of fact by the District Court that the surrounding circumstances showed the parties intended an absolute undertaking by the Builder and Respondent Surety directly to Petitioner.

It is disturbing to find that the Circuit Court of Appeals adopted this inconsistent attitude in the face of the fundamental rule that the contracts of paid sureties shall be construed strictly against them.

The rationalization by the Circuit Court of Appeals of this obvious inconsistency to the benefit of the Respondent Surety might possibly be said to be based on a misconstruction of the decision of the Pennsylvania Supreme Court in *Young* v. *American Bonding Company, supra,* and a further misconstruction of the general rule as to the proper mode of interpretation of contemporaneous instruments. However, two wrongs do not make one right. Either the Court should have applied the rule of strict construction throughout, and in doing so found that the condition of the bond was absolute; or it should have held that the circumstances of the transaction were relevant and affirmed the judgment of the District Court on its findings of fact.

The fundamentally inconsistent reasoning applied by the Circuit Court of Appeals in these cases, to the benefit of the Respondent Surety and to the great pecuniary harm of the Petitioner, who advanced money in reliance upon Respondent Surety's promise, is so great that it constitutes a departure from the usual course of judicial procedure. If "the rule that contracts mean what they clearly say applies to *both* contracting parties", then this Court should grant a writ of certiorari so that that rule may be enforced.

CONCLUSION.

It is submitted that the Circuit Court of Appeals, by its decision in these cases, has violated Rule 52(a) of the Federal Rules of Civil Procedure and the decisions of this Court interpreting that Rule.

In addition to having rendered a decision in conflict with the decisions of this Court, the Circuit Court of

APPENDIX.

OPINION.

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

No. 15270. March Term, 1930.

Provident Trust Company of Philadelphia

v.

Metropolitan Casualty Insurance Company of New York.

(Filed June 8, 1944.)

Before (s) KIRKPATRICK, *J.*

This is one of two civil actions which were tried together to the Court without a jury. The two actions are against a surety company and are based upon three bonds of a type commonly known as completion bonds, given in connection with three building operations, referred to respectively as the Furman, Roehm and Storck operations, those being the names of the three builders. The bonds are essentially alike and the two cases present the same questions of law, the only difference being that in the first case (Furman and Roehm bonds) the plaintiff sues in its individual capacity and in the second case (Storck bond) as trustee. As a matter of convenience the Furman operation will be considered, it being understood that the discussion, except as noted, applies equally to the other two operations.

The operation was undertaken by, or through the medium of, a corporation named Equitable Bonded Mortgage Company which, with a wholly owned subsidiary, Equitable Securities Corporation, was in the business of financing such operations, either by purchasing mortgages on the lots upon which houses were to be built or by lending money upon the security of such mortgages. The financing in this case was accomplished by means of the following (apparently) successive steps:

(a) A contract between the builder and Equitable, called an "operation agreement" which provided, among other things, that mortgages would be placed upon 20 of the lots, that a house would be constructed upon each according to agreed plans and specifications, that the mortgages would be transferred to Equitable and that Equitable would supply the money to the builder as the work proceeded. (b) The creation of the mortgages by the builders and their delivery to Equitable. (c) A bond given by the builder as principal, with the defendant as surety, to Equitable and its subsidiary for the completion of the houses. (d) Tender by Equitable to the plaintiff of its note in the amount of $112,000, the 20 mortgages, assigned to the plaintiff, and the defendant's surety bond assigned by Equitable to the plaintiff, accompanied by the defendant's written consent to the assignment. (e) The advance by the plaintiff to Equitable of $112,000.

The operation agreement, the mortgages and the assignments of them to Equitable and by Equitable to the plaintiff, the defendant's bond, its assignment by Equitable to the plaintiff, and the defendant's consent thereto all bear the date of October 15, 1928, and, as a matter of fact, the whole transaction was consummated on that day, except that the plaintiff advanced the money from time to time as required. Before (Stipulation Par. 3) the defendant's bond was delivered to Equitable, an assignment of it by Equitable to the plaintiff had been executed and the defendant had placed its written consent upon the instrument of assignment. The bond and assignment, with a statement of the defendant's financial condition and a power of attorney authorizing the execution of the bond, were bound together and backed by a single office backer of the defendant. In that form they were presented to the plaintiff together with the mortgages and Equitable's note.

It is undisputed that the houses were never completed (in fact, they were scarcely begun) that Equitable's note is unpaid and worthless, that the plaintiff realized the sum

of $150 from the sale of the mortgages, that no recovery can be had from the builder, that had the houses been completed the plaintiff would have been amply protected and that unless the plaintiff can hold the defendant upon its bond it will lose most of its loan.

The bond names Equitable and its subsidiary as the obligees. It recites and identifies the operation agreement between the builder and Equitable and the agreements of Equitable and its subsidiary to advance money for the work to be secured by assignment of first and second mortgages on the houses. The condition is as follows, "That if the buildings hereinabove mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to, and herein incorporated with like force and effect as if attached hereto, free and clear if (sic) mechanics' liens and municipal claims, within twelve (12) months from the date hereof, then this obligation to be void; or else to be and remain in full force and effect."

The surety's defenses are:

1. That the builder having been excused from performance by Equitable's default in failing to advance money for the buildings as it had agreed to do in the operation agreement and the principal therefore not being liable, the surety could not be held by Equitable, and hence cannot be held by the plaintiff, which, the defendant says, is nothing more than an assignee of a defaulting obligee, with rights no broader than those of its assignor. Note. It is an undisputed fact that Equitable never advanced any money to the builder for the construction of the houses, and it may be accepted as a fact that that was the reason the houses were not built and that, as between himself and Equitable, the builder would have been excused from performing by the failure of Equitable to advance the money or, as the defendant describes it, failure of consideration.

2. That Equitable and its subsidiary are joint obligees, and that default on the part of the subsidiary, the second

mortgage, which did not join in the assignment of the bond to the plaintiff is fatal to the rights of Equitable or any assignee of Equitable, regardless of any rights which the plaintiff might still have, had Equitable been the only obligee.

3. That the plaintiff lost its rights against the surety, because

(a) Its sale of the mortgage after default carried the right to recover on the surety bond, which, the defendant says, was given as security for the mortgages only, and so the sale divested the plaintiff of all further interest in the surety bond.

(b) The subsequent satisfaction of the mortgages paid the debt and released the surety.

(c) The renewal, before default, by the plaintiff of Equitable's six months note for a further period of six months, was an extension of credit which released the surety.

4. That the plaintiff has failed to prove damages.

5. That the plaintiff has lost its rights by abandonment and delay in prosecution.

At the center of the entire controversy, decisive of the issue raised by the first two defenses and directly affecting the third and fourth, lies the question whether this is a bond for the faithful performance of a contract (the operation agreement) or a bond for the completion of houses. If the former, the position taken by the surety in its first two defenses has, at least, technical merit. If the latter, it has none at all.

The defendant relies upon Young *v.* American Bonding Co., 228 Pa. 373. In that case the condition of a bond in terms similar to but not identical with those in the present case was construed in connection with the recitals (which referred to portions of a contract roughly corre-

sponding to the present operation agreement) to cover the faithful performance of the entire contract, including details of financing, and the Court held that a material alteration to the detriment of the surety in some of the financing provisions released the surety.

I do not think that Young *v.* Bonding Co. rules the present case.

The difference in the wording of the conditions of the two bonds may be noted. It is slight but not entirely without significance. In the Young case the condition was, "if the said principals shall well and faithfully construct and complete . . .." In the present case the condition is, "That if the buildings hereinabove mentioned shall be fully constructed and completed . . .."

But regardless of similarities or dissimilarities in the two bonds, the evidence shows that the transactions of the Young case and the present case, of which the bonds in the two cases formed part, were fundamentally entirely different, a fact which compels a different construction of the condition of this bond.

There is no doubt about the principle of the Young case that the recitals of a bond may properly be referred to in order to ascertain the scope of the condition. But the recitals are not always conclusive, and the Young case does not decide that they are. In construing the condition of a bond, the circumstances, including the nature of the transaction as a part of which it was given, are to be taken into account. If, when the entire transaction is considered it appears indisputably that the intention was to give the surety's absolute undertaking, disassociated from other contract obligations, that certain buildings would be completed then the condition must be so construed, though the recitals contain a reference to the other provisions of the contract. This, I think, is what appears in the present case.

I have described the form in which the transaction was cast. The substance of it was this:

Equitable and the builder, for their mutual profit, proposed to engage in a venture, consisting of the building of houses, for which money, in the amount of $112,000, was needed. It was found to be necessary, convenient or desirable to borrow from the plaintiff, which was willing to lend the money on the security of the land if, and only if, it could be assured by a corporate surety bond that houses would be built upon the land and completed in accordance with the plans. The plaintiff had no interest whatever in who got the money or how it was used. If the bond was adequate and the obligation honored, nothing the parties to the operation agreement might do or fail to do would affect the security of the loan. The defendant executed its bond with the condition that the houses would be built. The defendant knew the money for the operation was coming from the plaintiff and that the bond was going to be offered as security. And it must have known, from the dates which the documents bore and the fact that its bonds was delivered to Equitable already assigned to the plaintiff, if from nothing else, that the transaction was not and was never intended to be a series of distinct steps but was simply a borrowing from the plaintiff upon collateral which included the bond. With this knowledge it accepted the premium and delivered the bond, upon the faith of which, primarily, the plaintiff advanced the money.

Only on paper was Equitable ever an obligee. It never took anything but a remote and contingent interest in the bond, an interest which could attach only after the plaintiff had been paid in full, and, as a matter of fact, that never happened. Its position, if it be necessary to assign it a position, was in reality that of principal along with the builder. The subsidiary was Equitable's creature, and the legal fiction of a separate corporate existence for it cannot change the realities of the situation. It would be idle to pretend that Equitable's acts were not the acts of the subsidiary and that, so far as the plaintiff in this transaction was affected, the two corporations were not one and the

same. (Defendant's fifth request for finding of fact, affirmed by the Court.)

The defendant's position is a stand upon the technical aspect of the transaction. To sustain it would result in giving to Equitable, which received the plaintiff's money and which was one of two parties ultimately to benefit by it, a status which would allow it to dissipate the money or appropriate it to its own purposes, and by so doing, at one and the same time prevent completion of the houses and destroy the plaintiff's right to realize upon its security. To state that proposition, it seems to me, is to answer it.

The defendant contends that the parol evidence rule forbids the Court to look through the paper screen and view the transaction as it really was. This, however, is not so. If the language is not free from doubt (and it is certainly not free from doubt in the present case) then the circumstances surrounding the making of the bond and particularly the purpose for which it was given, should be taken into account. Purdy v. Massey, 306 Pa. 288, 293. But even where language is plain and unambiguous, there are many situations in which circumstances may be resorted to to show that a transaction is, in reality, something entirely different from what it appears to be. For example, a clause expressly stipulating for liquidated damages may be shown to be a penalty. A transfer, absolute on its face, may be shown to have been given for security only. A document purporting to be a bailment lease will not prevent the Court from holding the transaction a conditional sale if such it was in fact.

In Purdy v. Massey, supra, the Court considered the entire transaction of which the bond was a part and, holding that the wording of the condition was not free from doubt, said, "In this case such considerations (the circumstances surrounding) lead to but one conclusion—that this bond was an absolute undertaking to . . . complete the building." That this statement was not dictum appears from the fact that the Supreme Court overruled two assign-

ments of error which squarely raised the point that the plaintiff, although she had shown failure to complete the building, had failed to show that it was by reason of default on the part of the principal.

So considered I find that the bond in this case was an absolute undertaking by the defendant directly to the plaintiff that the houses would be completed according to plans and specifications identified by reference to the operation agreement, that it was intended solely to secure the plaintiff's loan and was not intended to and did not guarantee full performance of the operation agreement, that it was not intended to and did not confer any rights (except contingently on full payment to the plaintiff) upon Equitable or its subsidiary, that the plaintiff was the real obligee and that no default on the part of the nominal obligees would affect the plaintiff's rights.

Therefore, it is wholly immaterial whether or not default on the part of Equitable or its subsidiary excused the builder from his obligation under the operation agreement. The plaintiff having acquired its right against the surety, not derivatively by assignment from Equitable but directly by virtue of its advances of money on the faith of the note, mortgages and bond, it is also immaterial that Equitable's subsidiary did not join in the assignment and its default (even if that could be considered its separate act) is no defense.

The third defense if supportable at all must be upon the theory that the surety bond was given solely as collateral security for the assigned mortgages. Again, I am unable to take the defendant's view of the transaction. The mortgages were pledges; the bond was collateral security in the broad sense of an obligation running alongside of the principal debt, according to the derivational meaning of the word "collateral." Both were given to secure the loan. On default, the bank had the right to look to all the collateral which it held or to any of it. Jennings v. Loeffler, 184 Pa. 318; Adelphia B. & L. Assn. v. Trilling, 121 Pa. Sup.

469; Stoflet v. Kress, 342 Pa. 332. The sale of the mortgages exhausted the plaintiff's rights against that particular group of collaterals and what happened to the mortgages thereafter, whether they were paid or released or satisfied, made no difference. But it did not carry the plaintiff's rights in the bond nor divest the plaintiff of its right to enforce the defendant's obligation to make good the loss. This result could have followed only if the bond had been given solely as collateral for the mortgages, and it would need evidence of a very different kind of transaction from that appearing here to compel that finding.

The argument that the renewal of the notes released the surety is fully met by the rule of Philadelphia to Use v. Fidelity and Deposit Co. of Maryland, 231 Pa. 208; Trustees of Methodist Episcopal Church of Franklin v. Equitable Surety Co., 269 Pa. 411, and other cases, holding that a paid surety will be relieved only if the extension or alteration in the terms of the contract is material and work to its disadvantage. There is nothing in the present case to show that the defendant incurred any detriment by reason of the notes having been renewed, and as a matter of fact, nothing to show that it suffered any loss by reason of the mortgages' sale, assignment and foreclosure.

In addition to the foregoing, the assertion of this (third) defense is plainly an attempt by the defendant to "mend its hold." "Where a party gives a reason for his conduct and decision touching anything in controversy, he is estopped, after litigation has begun, from changing his ground and putting his conduct upon another and different consideration," Railway Co. v. McCarthy, 96 U. S. 258. Even before formal notice of default, the defendant repudiated and denied all liability with respect to the bond and the one and only reason advanced to justify its position in so doing was its first defense, already considered. It reasserted this position ("in accordance with our former correspondence") after it had

been notified by the plaintiff of its intention to sell the mortgage collateral at auction and after it had been advised of such sales of the Furman and Roehm mortgages and the Storck bonds. As late as February 26, 1943 the defendant filed its affidavit of defense on the merits with new matter and made no suggestion of this third defense.

The fourth defense is without merit. The measure of damages is the cost of completion (Purdy v. Massey, supra; Leonard's Estate, 343 Pa. 198). There is evidence of the estimated cost of the entire operation, including an intemized breakdown of the estimated cost of the buildings. This latter, taken in connection with the stipulation as to what had actually been done when work stopped, furnishes satisfactory evidence of so much of the cost as is applicable to the partial performance, from which the balance or cost of completing the unfinished job can be ascertained by simple subtraction.

The fifth defense was fully considered on the defendant's motion to dismiss and the conclusion reached that the record as then presented failed to show any evidence of abandonment of its cause of action by the plaintiff and that the history of the proceeding did not require an involuntary dismissal for want of prosecution. Discovery procedure taken by the defendant in preparation for trial has not produced any additional support for its position. Whether it intends to press this defense any further, I do not know, but no request raising it has been presented.

The defendant objected to the entire testimony of the plaintiff's vice-president "for the reason that it is our position that the transaction between the Provident and the Equitable is not relevant to the issue before your court." Having held in the foregoing opinion that the transaction was relevant, I overrule the objection. Later in the witness' testimony various other objections were interposed none of which have any substantial merit and they are overruled. The rule against leading questions

has long ago been relaxed to permit the Court to exercise a sound discretion, in the interest of expediting the proceedings and clarifying the testimony where, in the Court's judgment, it can be done without danger of falsehood.

The plaintiff's vice-president testified that, without the bond, the loan would not have been made. While this testimony was properly received, I may say that it is a fact which I would find from the circumstances, entirely independently of the testimony.

ANSWERS TO REQUESTS.

The stipulation of facts is adopted as the Court's special findings of fact. The view taken by the Court of the nature of the transaction involved in the case makes a number of facts stipulated immaterial and this also applies to a number of the defendant's requests. Such requests as are not covered by the facts as found above are held to be immaterial and are not answered. The statements of fact in the opinion may be taken as additional special findings, supplementing or modifying the facts as stipulated, and answering such requests as are not covered by the stipulation. The statements of law contained in the opinion may be taken as conclusions of law.

I affirm the plaintiff's requests for conclusions of law and deny the defendant's except the first which I affirm.

An order for judgment in accordance with the foregoing may be presented.

15272

Before (s) KIRKPATRICK, *J.*

This action was upon the bond in the Storck operation which, in point of time, was the earliest of the three. The only difference between this action and No. 15270 is the fact that in the Storck transaction the builder's

application to the defendant for the surety bond contains the question and answer, "To whom to be given?" "Provident Trust Co., Trustee."—a fact which makes the defendant's knowledge of the real nature of the transaction even plainer than in the other case.

The facts and legal principles stated in the opinion in Action No. 15270 may be taken as special findings and conclusions in this one. In addition I affirm the plaintiff's requests for findings of fact and conclusions of law. It is unnecessary to answer such of the defendant's requests for findings of fact as are not covered by the foregoing, the reasons stated in No. 15270 being applicable. I deny all the defendant's requests for conclusions of law except the first, sixteenth and seventeenth, which are affirmed.

An order for judgment for the plaintiff may be presented.

OPINION

OF THE

UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

No. 15270.

Sur Motion for New Trial.

Before KIRKPATRICK, *J.*

This case turned mainly upon the scope of the defendant's obligation—whether the bond was for the faithful performance of the building contract or for the completion of the houses, regardless of reasons or excuses for their non-completion. The court found that it was the latter kind of bond.

In reaching its conclusions the court examined the entire transaction and found that the bond was intended to run directly to the plaintiff to secure its loan, the plaintiff being the real obligee, that the building operation had been

undertaken by, or through the medium of, Equitable Bonded Mortgage Company and that Equitable, although on paper an obligee, was in reality and to the knowledge of the plaintiff in the position of a principal along with the building contractor (the nominal principal). The defendant's chief contention in this motion for a new trial is that this view of the transaction was a pure figment of the court's imagination without anything in the record to warrant it.

Ample evidence supporting the court's findings is to be found in the stipulation, testimony, and exhibits, which fully disclose the circumstances surrounding the transaction, the manner in which it was consummated, the relationships of the various parties to it and their common knowledge of the objects to be attained.

However, it is also worth noting that the defendant itself is on record in the case with an explicit avowal that the real, as distinguished from the apparent, relationship of the parties was what the court found it to be. In the affidavit, filed in support of a motion to dismiss the action for want of prosecution and expressly incorporated in the written motion presented by the defendant's counsel, the following appears, "The said principals designated in the said bonds were in fact only straw parties acting on behalf of the said obligees which controlled the actions and operations of the said principals and such method of operation by the obligees was or should have been known to the plaintiff herein at the time of the assignment of the said bonds by the said obligees to plaintiff herein." It is also alleged that certain witnesses, if living, would have testified "that the said operations were actually the operations of the obligees (Equitable) designated in the said bonds, that the contractors in whose names the applications for the surety completion bonds were submitted, were actually dummy contractors working for and on behalf of the said obligees;" etc. The court did not go quite so far as to characterize the contractors as dummies, but, otherwise, the foregoing quotations epitomize

the court's view of Equitable's position in the transaction, and could have been adopted, in hæc verba, as one of the findings.

Although the court did not have this affidavit in mind in making the findings, he might well have considered it, under general principles relating to judicial notice. See U. S. v. City of Philadelphia, C. C. A. (3), 140 F. 2d 406; Perlman v. 322 West Seventy-Second Street Co., Inc., 127 F. 2d 716. The motion was more than a mere procedural step. Upon the facts asserted in it the defendant sought to persuade the court to dismiss the whole cause. In view of what appears in it, it is pretty hard to see much force in the argument which the defendant now makes that the view which the court took was wholly unwarranted, unexpected and prejudicial.

None of the other reasons presented in support of the motion has enough substantial merit to call for the granting of a new trial.

The motion is denied.

Sur Motion to Amend Findings.

The court did not intend to disurb or modify the stipulated facts in any particular, and the findings appearing in the opinion do not have that effect. In order to avoid any misunderstanding which the defendant may have upon the point, the opinion is amended by striking out the word "stipulated" in the third line of the last page and substituting the words "separately found." One or two other minor changes in the opinion heretofore made by the court are confirmed. The court amends its affirmance of the plaintiff's second request for conclusions of law by allowing interest at 3 percent instead of 6 percent, in order to conform with the court's later memorandum sur motion for judgment.

Sur Motion to Amend Judgment.

The motion is denied.

UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 8846 and 8847 October Term, 1945

PROVIDENT TRUST COMPANY OF PHILADELPHIA, a Corporation of the Commonwealth of Pennsylvania

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK, a Corporation Existing Under the Laws of the State of New York,

Appellant

APPEALS FROM THE JUDGMENTS OF THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

Argued October 5, 1945
Before ALBERT LEE STEPHENS, MARIS and GOODRICH,
Circuit Judges.

OPINION OF THE COURT
(Filed December 17, 1945)

By GOODRICH, *Circuit Judge.*

This case arises on appeal from two District Court judgments,[1] against a surety on three completion bonds in the aggregate amount of $868,264.79. Both cases are factually alike and present identical questions of law.[2] The persons involved are: Provident Trust Company of Philadelphia, plaintiff; Metropolitan Casualty Insurance Company of New York, defendant; and Equitable Bonded Indemnity Company with its wholly owned subsidiary, Equitable Securities Corporation. From the business operations of the Equitable companies with certain builders, Furman, Roehm and Storck, and their surety, the defendant Metropolitan, on the one hand, and the plaintiff Provident on the other, the present conflict of interests arose.

The case is in Federal Court on diversity grounds only. All the operative facts seem to have had their setting in Pennsylvania. Under the now well understood and established rule, Pennsylvania law is to be applied and Pennsylvania decisions, so far as found to be applicable to the questions in the case are controlling.[3]

The defendant's principal and most important point, while presented with considerable elaboration, brings the case down to a simple set of facts which, in turn, is controlled by simple and well settled propositions of law. The substance of the case on the defendant's theory is this: A builder undertakes certain operations. In the

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[1] One judgment was for $457,012.31 representing the full amount of two unpaid loans less a credit of $300 plus 3% interest for a little over 15 years; the other judgment was for $411,252.48 representing the full amount of Debenture Bonds, less a credit of $200 plus 3% interest for more than 15 years.

[2] The purely nominal difference is that in one case, plaintiff sues in an individual capacity on two of the bonds, and in the other case, it sues as trustee on the remaining bond.

[3] The decision referred to by appellee as presenting a case (Baglin v. Title Guaranty Surety Co., 166 Fed. 356, affirmed, 178 Fed. 682 (C.C.A. 3, 1909)) "so nearly identical" was decided long before Erie R. Co. v. Tompkins was ever dreamed of. A Federal Court decision upon a question of state law settled upon principles of "general commercial law" is no precedent now.

language of suretyship, he is the principal debtor. He is to be supplied with money by a creditor, in this instance Equitable. A completion bond is given by the defendant surety. With the consent of the principal debtor and surety, rights of the creditor (Equitable) are assigned to plaintiff Provident Trust Company. The principal debtor's project is never completed because the creditor (Equitable) fails to advance the funds promised. This failure excuses the debtor from its performance.[4] Since the principal debtor is not in default upon his performance, his surety is likewise not in default. Therefore the creditor (Equitable) cannot recover against the surety.[5] Provident is but the assignee of the creditor and the rights of the assignee rise no higher than the assignor.[6] Judgment must, therefore, be for the defendant. If the defendant is right in its argument that the facts in the instant case are essentially those in the statement just made, it is perfectly clear that it is right in its legal conclusion. Indeed, the plaintiff would not claim to the contrary.

The plaintiff, however, claims and got the District

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[4] Restatement Contracts, § 274(1) "In promises for an agreed exchange, any material failure of performance by one party not justified by the conduct of the other discharges the latter's duty to give the agreed exchange even though his promise is not in terms conditional." Pennsylvania Annotations § 274(1), in accord, cites a great variety of cases.

[5] Restatement Security § 126 "Where there is a promise for an agreed exchange between creditor and principal and there is a material failure of performance by the creditor not justified by the conduct of the principal, the surety is not liable to the creditor unless the principal has elected to treat the failure only as a partial breach." Pennsylvania Annotations § 126, *"Accord:* Gunnis v. Weigley, 114 Pa. 191, 6 A. 465 (1886)". See also: McShain v. Indemnity Insurance Company of North America, 338 Pa. 113, 12 A. (2d) 59 (1940); Young v. American Bonding Company, 228 Pa. 373, 77 A. 623 (1910).

[6] Restatement Contracts § 167(1) "An assignee's right against the obligor is subject to all limitations of the obligee's right, to all absolute and temporary defenses thereto and to all set-offs and counterclaims of the obligor which would have been available against the obligee had there been no assignment, provided that such defenses and set offs are based on facts existing at the time of the assignment, or are based on facts arising thereafter prior to knowledge of the assignment by the obligor". Pennsylvania Annotations § 167(1) in accord, cites a number of cases.

Judge to go along with the claim, that it is not the assignee of a contract made by the defendant with Equitable but the contract is essentially one with the plaintiff itself. Its rights are not, therefore, derived by assignment from Equitable, but are obligations running directly from defendant to plaintiff. Of course, if this is the substance of the transaction, the view set out above has no application. There were no conflicts of testimony to be resolved at the trial. Most of the facts were stipulated and the testimony of the one witness, A. G. Scattergood, Vice-President of the plaintiff, was not disputed but relied on by the defendant. Our question becomes, therefore, what is the legal conclusion to be drawn from facts rather than what are the facts themselves.

Are the plaintiff's rights based on an obligation running directly to it or do they arise only by assignment from Equitable? Plaintiff contends,[7] and the District Court agreed, that Provident was a direct obligee. The facts upon which this conclusion is based are these: the surety knew that Provident and not Equitable was to be the ultimate recipient of the bonds;[8] the bonds, assignment and consent to assignment were bound together as though they were a single document;[9] the whole transaction was consummated in a single day (except for advances of money) so that Equitable was only a fleeting holder of the instruments which were immediately transferred to Provident; the assignment was executed and consented to even before the bonds were

[7] Plaintiff's theory is that the "primary purpose of the surety bonds was to protect Provident" and "the 'assignment' in the bonds was an 'assignment' in name only".

[8] The District Court points out that "* * * in the Storck transaction the builder's application to the defendant for the surety bond contains the question and answer, 'To whom to be given?' 'Provident Trust Co., Trustee'—a fact which makes the defendant's knowledge of the real nature of the transaction even plainer than in the other case." The Court adds, "The plaintiff's vice president testified that, without the bond, the loan would not have been made."

[9] The single document view rests on this in the District Court's own wording: "The bond and assignment, with a statement of the defendant's financial condition and a power of attorney authorizing the execution of the bond, were bound together and backed by a single office backer of the defendant."

delivered to Equitable;[10] and finally defendant's statement that the principals were straw men.[11] This we think is a fair summary of the points relied upon by plaintiff and sustained by the District Court to show an obligation direct to plaintiff.

But since we are here dealing with obligations arising out of words used by the parties, we had better give attention to the language they used, unless we are to put the cart before the horse. If that language is ambiguous, we may, of course, go behind it and examine the cartload of surrounding facts to try to find out what was meant. As might well be expected of large financial organizations skilled in their calling, and advised by able counsel, the language is clear and to the point. It is plainly the language of assignment. The bonds refer to Equitable and its subsidiary as "obligees". The assignments say that Equitable does "grant, bargain, sell, transfer, assign and set over" to Provident. They speak of the bond "so assigned" and of "this assignment" to Provident. They provide that if the mortgages be reassigned to Equitable, Provident will also "re-assign" its rights under the bond. Metropolitan and the builders state, "We hereby consent to the above assignment." The pleadings by Provident

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[10] This does not amount to a technical flaw in the assignment, however. For while the assignments and consents were executed before the bonds were delivered to Equitable, that delivery nonetheless preceded delivery of the assignments to Provident. Thus when the documents were handed to Equitable the bonds became effective by delivery and when "thereafter" as is stipulated, the documents were handed to Provident the assignment became effective by delivery. And in any event, even if the assignment had become effective before the bonds were delivered, the latter would still have been assignable as future interests. East Lewisburg Lumber & Mfg. Co. v. Marsh, 91 Pa. 96 (1879); Ruple v. Bindley, 91 Pa. 296 (1879); Citizens Trust & Surety Co. v. Howell, 19 Pa. Super. 255 (1902).

[11] The District Court states, "In the affidavit, filed in support of a motion to dismiss the action for want of prosecution and expressly incorporated in the written motion presented by the defendant's counsel, the following appears, 'The said principals designated in the said bonds were in fact only straw parties acting on behalf of the said obligee which controlled the actions and operations of the said principals and such method of operation by the obligees was or should have been known to the plaintiff herein at the time of the assignment of the said bonds by the said obligees to the plaintiff herein'."

speak of defendant surety having "executed its written consent to a certain written assignment" to plaintiff. It is further expressly stipulated that Metropolitan as surety and the builders as principals, "executed their written consent to a certain written assignment to Provident." And the plaintiff sues as assignee of a contract, not one praying for reformation of an instrument. This is clear, exact, accurate. Neither we nor Judge Learned Hand's twenty bishops could change its plain meaning.[12] We have no case of mistake here, nor reliance by one party on the superior skill or knowledge of the other, no dominant bargaining agency which has imposed its will on a weaker party by hiding the real nature of the transaction through language formed to its own advantage,[13] nor any other possible reason for disregarding a simple meaning clearly expressed.

Furthermore, we do not see that the various facts urged by the plaintiff to show that Provident was a direct

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[12] Judge Learned Hand in Hotchkiss v. National City Bank of New York, 200 Fed. 287, affirmed 231 U. S. 50 (1913): "A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent. If, however, it were proved by twenty bishops that either party when he used the words, intended something else than the usual meaning which the law imposes upon them, he would still be held, unless there was some mutual mistake, or something else of the sort."

[13] The District Court states, "But even where language is plain and unambiguous, there are many situations in which circumstances may be resorted to to show that a transaction is, in reality, something entirely different from what it appears to be." It cites as examples that a clause for "liquidated damages may be shown to be a penalty"; a "transfer, absolute on its face, may be shown to have been given for security only"; and a purported bailment lease shown to be a conditional sale. In all these instances courts cut through the transaction as the parties have written it. The purpose of forbidding a clog upon the equity of redemption is of course to protect a debtor against a dominant creditor. In the liquidated damage case there is the same element of public policy present plus the point that when parties are allowed to stipulate for damages at all they are, to some extent, substituting their own rules for those of the law. Obviously this is a privilege to be kept within limits. All these exceptions are inapplicable here, for this is but an ordinary bargain between strong and well advised business concerns. So long as they stay within the law they may deal as they please and neither needs the guardianship of a court.

obligee prove the conclusion. It was quite probable that Provident considered itself sufficiently protected as an assignee. The testimony of its vice president showed the company sometimes took obligations running directly to it. We have no doubt that in fact its officers knew the difference. We think the binding of all papers together is not a legally significant fact nor is the length of time Equitable held them before handing them over to Provident. The matter of the affidavit referred to above does not come within what has been said. It should be noted however that this was filed at an early stage in the proceedings among matters "intended to be proved" by defendant. It was before the answer and before the stipulations the parties entered into. We think it has no significance. Further, except for mutual mistake and reformation, the rule that contracts mean what they clearly say applies to both contracting parties.

There is one more problem which requires consideration. The plaintiff claims that the surety's obligation was an absolute one. It points out that the language of the condition of the bond is that "The buildings hereinbefore mentioned shall be fully constructed and completed in accordance with the plans and specifications above referred to." This, it says, is an absolute and unconditional promise to see that completion is accomplished. In Purdy v. Massey, 306 Pa. 288 (1932) the Supreme Court of Pennsylvania was discussing language in a completion bond and its problem was whether the language used by the surety constituted the promisor a guarantor or whether the promise was merely to indemnify. The court concluded that the language was an affirmative covenant to "complete the building in the event of default by the principal". It was found that there was default by the principal and the surety was held. But the court was not holding the surety as anything more than a guarantor of performance by the principal debtor.

Of course, it is possible for a surety to contract that

a thing will happen or that a given result shall be produced. We think it likely that ordinarily surety bonds are not so given because the ordinary concept of suretyship is that of one person backing up the performance of another.[14] The question is whether this particular bond, in the language quoted, creates a promise on the part of the defendant regardless of the default of anyone else. The surety company relies upon the Pennsylvania decision of Young v. American Bonding Company, 228 Pa. 373, 77 A. 623 (1910). The plaintiff strenuously urges that this case is not in point and the District Court was led to agree with it.[15] If the Young case is in point we think it establishes the proposition that the words used in this type of bond which, in turn, contains a reference to a contract, makes performance of the surety's promise conditioned upon the non-performance of the main contract by the principal debtor. If this case is in point it obviously governs us because, as stated above, the instant case is to be settled in accordance with Pennsylvania law. We quite realize that it is part of a mature system of law to make distinctions. Only an exceedingly primitive legal culture is unable, for instance, to distinguish between intentional killing and death through accident. But it is not part of a mature system of law to make distinctions without differences. We cannot see, upon this point, any difference between the American Bonding case and this one. We think the former decision controls. The conclusion of that control is that the defendant's liability was conditioned upon a default by the principal obligor, that is the builder. The builder was not in default because

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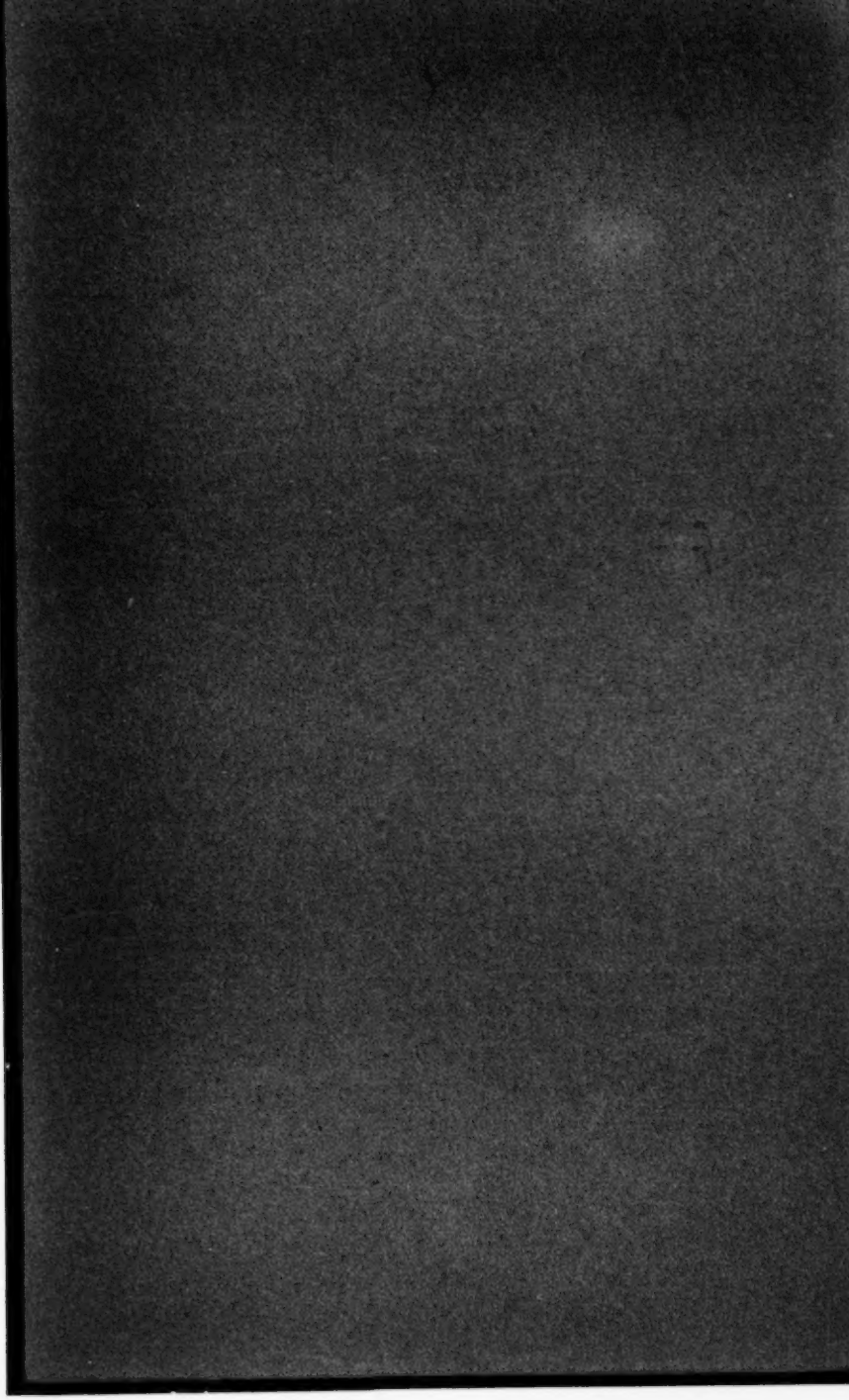
[14] See Restatement Security § 82 and Comment thereto.

[15] The District Court says it does not think the Young case rules because: "The difference in the wording of the conditions of the two bonds may be noted. It is slight but not entirely without signfiicance. In the Young case the condition was, 'if the said principals shall well and faithfully construct and complete . . .'. In the present case the condition is, 'That if the buildings hereinabove mentioned shall be fully constructed and completed . . .'." The Court goes on to point out that the subsidiary facts of the Young case and the instant case are also "fundamentally entirely different".

he had an excuse for non-performance. Neither is the surety.

This analysis of the case makes it unnecessary for us to consider the other arguments made by the defendant.

The judgments of the District Court are reversed.



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IN THE

Supreme Court of the United States.

October Term, 1945
No. 815

PROVIDENT TRUST COMPANY OF PHILADELPHIA,

Petitioner,

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK,

Respondent.

October Term, 1945
No. 816

PROVIDENT TRUST COMPANY OF PHILADELPHIA, TRUSTEE,

Petitioner,

v.

THE METROPOLITAN CASUALTY INSURANCE COMPANY OF NEW YORK,

Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION.

JURISDICTION.

The judgments of the Circuit Court of Appeals in both cases were entered December 17, 1945. Petitioner invoked jurisdiction of this Court under Section 240 (a) of the Judicial Code (U. S. Code, Title 28, Paragraph 347).

QUESTIONS PRESENTED.

1. When documents are clear and unambiguous, will the Court determine the rights and duties of the parties as a matter of law, in the absence of fraud, accident or mistake?

(*Affirmed by the Circuit Court.*)

2. Are the rights of the petitioner those of an assignee?

(*Affirmed by the Circuit Court.*)

3. Is the surety on a completion bond liable to the assignee of a defaulting obligee where the principal is free from fault?

(*Negatived by the Circuit Court.*)

STATEMENT.

The two cases were tried together, and the applications for certiorari raise the same questions. Respondent is therefore filing the same brief in both cases. There were three building operations and three sets of documents, alike in form, with three different builders, Martin Furman, Herbert Roehm, and Jesse Storck. The documents and facts in the Furman building operation are used in the Statement and in the Argument.

These suits were filed on March 7, 1930. They were tried by the District Court, without a jury, on December 2, 1943.[1]

The documents upon which the petitioner sues consist of the surety bond and of the assignment on which is the consent to assignment. In addition to these and other documents, the evidence consists of stipulated facts, and the undisputed testimony of one witness.

Paragraphs 16 and 17 of the Stipulation of Facts [2] state the obligee's default and the principal's freedom from fault:

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[1] Reference is made to the Docket Entries for the history of these cases. Appendix, pp. 1a, 70a.

[2] Appendix 54a.

"16. Prior to May 31, 1929, Equitable Bonded Mortgage Company did not advance to Martin Furman, or any other persons, including labor and material men, moneys in the aggregate of $142,000 for the erection and completion of twenty dwellings on the Southeast side of Wadsworth Street between Anderson Street and Ardleigh Street, in the 22nd Ward of the City of Philadelphia, or for the purchase of, and to be secured by, assignments of twenty first mortgages thereon, described in the Operation Agreement, Defendant's Exhibit 17 and in the second recital of Defendant's Bond, Exhibit 'A' of Plaintiff's Statement of Claim, which first mortgages so described were created in the aggregate principal amount of $142,000 and were duly assigned and delivered to Equitable Bonded Mortgage Company; and subsequent to May 31, 1929, Equitable Bonded Mortgage Company advanced no moneys to Martin Furman or any other person or persons for said operation or mortgages."

"17. That Martin Furman, the principal named in Defendant's Bond, Exhibit 'A' of Plaintiff's Statement of Claim, prior to May 31, 1929, had not at any time repudiated his obligation under a certain written agreement, dated October 15, 1928, with the Equitable Bonded Mortgage Company, admitted into evidence as Defendant's Exhibit 17, and referred to in the said bond, Exhibit 'A' of Plaintiff's Statement of Claim, for the erection and completion of the dwellings identified in Paragraph 16 of this Stipulation, or done anything which amounted to a breach of his obligations under the said written agreement, or any act which constituted anticipatory breach of the same. Martin Furman and the labor and material men involved did not abandon the work of construction on the said building operation until after Equitable Bonded Mortgage Company ceased to furnish the funds agreed upon in the Operation Agreement, Defendant's Exhibit 17, and

recited in the Bond, Exhibit 'A' of Plaintiff's Statement of Claim."

The following additional facts relate to the business dealings between petitioner and Equitable.[3]

The business relations between petitioner and Equitable were extensive and pre-dated these transactions by several years.[4] Petitioner had confidence in the financial strength and responsibility of Equitable, and petitioner's Board of Directors authorized its officers to make collateral loans to Equitable up to $500,000 at any one time.[5] During the period from 1926 to 1929, Equitable was one of the larger borrowers from petitioner, perhaps the largest.[6] Petitioner made its loans to Equitable without imposing any restrictions on Equitable as to the use of the proceeds.[7] The petitioner, in previous transactions, had taken from Equitable assignments of surety completion bonds involving other principals and other sureties, which were in the identical form of the bonds and assignments used in the cases at bar.[8] In other transactions with Equitable, petitioner received bonds running directly from the builder and his surety to petitioner as the obligee, indicating that petitioner at times took a direct bond obligation and at other times merely an assigned bond obligation.[9]

In the instant cases, Equitable pledged first mortgages of the Furman operation with petitioner as collateral security for a loan, and assigned the Furman completion bond along with the mortgages. This loan was not made for the purpose of providing Equitable with funds to meet its obli-

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[3] "Equitable" is used throughout to designate "Equitable Bonded Mortgage Company."

[4] Appendix 137a, et seq.

[5] Stipulation of Facts 29, Appendix 59a.

[6] Testimony of Mr. Scattergood, Appendix 144a.

[7] Testimony of Mr. Scattergood, Appendix 155a, et seq., and Stipulation of Facts 28, Appendix 59a.

[8] Testimony of Mr. Scattergood, Appendix 150a, et seq.

[9] Testimony of Mr. Scattergood, Appendix 152a.

gation to any particular builder or building operation.[10] Equitable had full freedom to use the borrowed funds in any manner it desired. The petitioner also knew that Equitable and Equitable Securities Corporation were obligated to the builder for almost double the amount of petitioner's bank loan.[11] Petitioner did not conduct any part of its loan transaction with either the builder or with respondent, and there were no dealings of any kind between petitioner and respondent.[12]

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[10] Testimony of Mr. Scattergood, Appendix 155a.

[11] Testimony of Mr. Scattergood, Appendix 144a; Stipulation 26, Appendix 58a. For instance, the petitioner's loan to Equitable upon the Furman operation mortgages was only $112,000., but the obligations of Equitable to the builder, in the amount of $142,000., and of Equitable Securities Corporation, in the amount of $81,000., totalled $223,000.

[12] Testimony of Mr. Scattergood, Appendix 146a, 154a.

ARGUMENT IN OPPOSITION TO GRANTING OF THE WRIT.

I. The Circuit Court Properly Decided as a Matter of Law That the Petitioner's Rights Against Respondent Were Those of an Assignee.

In urging that the Circuit Court erred in holding petitioner to be an assignee, petitioner assumes that disputed issues of fact appear in the trial record and that the District Court resolved such issues of fact by its findings. Petitioner then argues that the Circuit Court refused to follow what petitioner claims are findings of fact by the District Court, and thereby violated Rule 52 (a) of the Federal Rules of Civil Procedure. Petitioner's assumptions are not correct.

The case was submitted on detailed stipulations of fact, the uncontradicted testimony of one witness, and the documentary evidence. There were no disputed issues of fact in the trial record. The only question for determination was the legal effect of the proven facts. This is a matter of law, not of fact. It is obvious that the Circuit Court is not precluded from determining a question of law merely because the District Court may have termed a legal conclusion a finding of fact.[13]

A. Interpretation of Unambiguous Documents is a Matter of Law.

Under the law of Pennsylvania the interpretation of an unambiguous contract is for the Court, not for the Jury. The following are clear judicial holdings to that effect:

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[13] Petitioner appears to argue to the contrary. "However, the Circuit Court of Appeals was not at liberty to nullify the effect of the trial court's finding by considering it in any light other than as a finding of fact." (*Petitioner's Brief, p. 16.*)

"Where all of the agreement or understanding between the parties is before the court in writing and it is unnecessary for any reason to resort to any evidence dehors the written contract, the court must construe the contract and not leave it to the jury for interpretation. . . . The construction of a written contract of employment is a matter of law."

Baldwin v. Magen, 279 Pa. 302, at 306, 123 Atl. 815 (1924).

"His [the plaintiff's] contention that this [the letter] was ambiguous is, in our opinion, wholly untenable. We cannot find in the letter any difficulty of construction which justified the trial judge in permitting plaintiff to testify as to his interpretation and in submitting to the jury the question of the reasonableness of such interpretation. We think that its language was plain, and that, therefore, as in the case of all written instruments, it was the function of the court to declare and apply its meaning."

Currie v. Land Title Bank and Trust Co., 333 Pa. 310, at 314, 5 A. (2d) 168 (1939).[14]

In the cases at bar, the language of the bond, of the assignment, and of the consent to the assignment, was clear and unambiguous, and not in dispute. Therefore, the interpretation of those instruments was for the Court in accordance with the above rule. Had there been a jury trial in the cases at bar, and had the trial judge submitted those instruments to the jury for interpretation, this would have been reversible error.

The questions in the instant cases are for the Court, and therefore the cases cited by the petitioner for the proposition that findings of fact shall not be set aside unless

[14]Accord: *Shafer v. Senseman,* 125 Pa. 310, 316, 17 Atl. 350 (1889); *Kelley v. Delaware, Lackawanna & Western Railroad Co.,* 270 Pa. 426, 428, 113 Atl. 419 (1921).

clearly erroneous are not applicable here.[15] For the same reason, Rule 52 (a) does not apply. As was stated by the Circuit Court of Appeals for the Fifth Circuit:

> "A copy of one of the certificates, the resolution authorizing their issuance and what has been done, since their issuance, with and in regard to them, appears in the evidence without contradiction or dispute. The case then is not one for the weighing of evidence, and the resolution of testimonial differences, and in which therefore, we must take the facts as the District Judge has found them, but one for the determination by us of the legal effect of the facts as the record

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[15]All the cases cited by petitioner involve findings of fact. In *McCaughn v. Real Estate Land Title & Trust Co.*, 297 U. S. 606, and in *Allen v. Trust Company of Georgia et al.*, 90 L. Ed. 305 (1946), the issue of fact was whether a gift had been made in contemplation of death. *Tennessee Coal Company v. Muscoda Local*, 321 U. S. 590, and *National Mutual Casualty Co. v. Eisenhower*, 116 F. (2d) 891 (C. C. A. 10, 1940) both involved factual determinations based upon extended, detailed and partially conflicting testimony. *Commissioner of Internal Revenue v. Scottish American Investment Company, Ltd.*, 323 U. S. 119, and *Boehm v. Commissioner*, 90 L. Ed. 96, came up from the tax court and the special provisions of the Internal Revenue Code and the rule of *Dobson v. Commissioner*, 320 U. S. 489 (1943), not Rule 52a, prevail. None of these cases involves the question of construction of written instruments which, as in the cases at bar, under Pennsylvania law is a matter of law for the court and not a matter of fact for a jury. *Biggs v. Mays*, 125 F. (2d) 693 (C. C. A. 8, 1942), was determined with special reference to Arkansas—not Pennsylvania—law. *Bogk v. Gassert*, 149 U. S. 17 (1893) and the Pennsylvania cases cited by Petitioner at page 17 are cases where, to prevent imposition and fraud, the Court inquired into the underlying agreement between the parties. See Opinion of the Circuit Court, Petitioner's Brief p. 20a and footnote 13 thereto.

presents them, clearly, simply and without controversy."

U. S. v. South Georgia Ry. Co., 107 F. (2d) 3 (C. C. A. 5, 1939).[16]

The Circuit Court for the Seventh Circuit stated the rule thus:

"Since the facts are not in dispute, we are free to consider them and to reach our own conclusion, untrammeled by the District Court's findings and conclusions of law. Especially is this rule applicable in the case at bar, where all the facts are stipulated."

Wigginton v. Order of United Commercial Travelers of America, 126 F. (2d) 659, 661 (C. C. A. 7, 1942); certiorari denied, 317 U. S. 636, 63 S. Ct. 28 (1942).

B. The Circuit Court correctly interpreted the documents.

It remains to consider whether the Circuit Court was correct in concluding that petitioner was only an assignee of Equitable and therefore subject to the defenses against Equitable.

Following the sound suggestion of the Circuit Court not to "put the cart before the horse,"[17] the writings themselves should be examined first. In the bond[18] Equitable and Equitable Securities Corporation are named as

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[16]Accord: *United States v. Mitchell*, 104 F. (2d) 343 (C. C. A. 8, 1939), "In this case no occasion arises for the application of the tests contemplated by either of said Rules to the findings of fact by the Trial Court. There is no conflict in the evidence. The evidence in relation to the claimed contract is all documentary." To the same effect, see *Kuhn v. Princess Lida of Thurn & Taxis*, 119 F. (2d) 704 (C. C. A. 3, 1941).

[17] Opinion of the Circuit Court, Petitioner's Brief, p. 19a.

[18]Appendix 15a.

obligees, Martin Furman, the builder, as principal, and respondent as surety. There is nothing ambiguous or uncertain in the naming of the parties and petitioner is nowhere mentioned. The language of the assignment [19] is that Equitable "does hereby grant, bargain, sell, transfer, assign and set over unto petitioner all of its right, title and interest in and to and right to recover under a certain bond." [20] It speaks of the bond "so assigned" and of "this assignment", and provides that under certain circumstances the petitioner would "re-assign" the bond to Equitable. This language is certainly unambiguous and does not purport in any way to vary the clear language of the bond. Finally, there was principal's and respondent's consent to the assignment which reads, "We hereby consent to the above assignment." [21]

The writings have been pleaded as and stipulated to be a bond, an assignment of the bond, and a consent to the assignment of the bond. There is no language in any of the instruments which suggests that they are anything else. Neither the petitioner nor the District Court has pointed to any language which supports the conclusion that petitioner, and not Equitable, was intended to be the obligee of the bond.[22] The Circuit Court concluded that the language was "clear, exact, accurate." [23] Nothing could be more obvious.

When instruments are as clear and unambiguous as these, their meaning must be determined from the instru-

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[19] Appendix 17a.

[20] Ibid.

[21] Appendix 18a.

[22] Although in the Questions Involved and in various portions of its Brief petitioner refers to Equitable as a "promoter" and as the "nominal" obligee it should be noted that such designations are wholly incompatible with the status of Equitable as disclosed by the pleadings and stipulations.

[23] Opinion of the Circuit Court, Petitioner's Brief, p. 20a.

ments themselves and, in the absence of alleged fraud, accident or mistake, courts will not go beyond the four corners of the instrument to determine the intent of the parties. The following statement from Corpus Juris [24] has been quoted with approval in Pennsylvania [25] and correctly states the law of Pennsylvania on the interpretation of written instruments:

> "The intention of the parties is to be deduced from the language employed by them, and the terms of the contract, where unambiguous, are conclusive, in the absence of averment and proof of mistake, the question being, not what intention existed in the minds of the parties, but what intention is expressed by the language used. When a written contract is clear and unequivocal, its meaning must be determined by its contents alone; and a meaning cannot be given it other than that expressed."

The Supreme Court of Pennsylvania has stated:

> "The object of interpretation and construction is, if there be any uncertainty as to the meaning of a contract, to find the intention of the parties. *If the contract is clear and unambiguous there is no room for construction. The parties, in the absence of fraud, accident or mistake, are bound according to the plain words of the contract.*" (Italics supplied.)
>
> *Shafer v. Senseman,* 125 Pa. 310, at 316, 17 Atl. 350 (1889).

The interpretation of surety bonds is no exception:

> "In other words, the liability of the sureties must be determined by the contract of the parties *as disclosed by the language of the bond.*

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[24] 13 C. J. pp. 524-525.

[25] *Nat. Realty Appraisal Co. v. Art Club,* 129 Pa. Super. 99, 195 Atl. 139 (1937).

"A bond, like any other contract, must be construed as to carry out the intention of the parties accepting and giving it. In the absence of fraud, accident or mistake, if the intention clearly appears from its terms its interpretation cannot be controlled by testimony dehors the instrument itself." (Italics supplied.)

Phoenix Mill Co. v. Kresge, 254 Pa. 36, at 41, 98 Atl. 772 (1916).

There has never been any claim of fraud, accident or mistake in the present case. There is no ambiguity in the bond, assignment, or consent to assignment as to who were the parties to the instrument and what were to be their rights and obligations. That being the case, the District Court was bound to follow the clear intention expressed by the language of those writings. That Court ignored the facts that Equitable and Equitable Securities Corporation are the obligees in the bond, that Equitable *assigned* its interest in the bond to petitioner, and that respondent consented to the *assignment,* and held that petitioner was the obligee of the bond. Under the Pennsylvania authorities a court may not ignore the clear unambiguous language of a writing. In doing so the District Court was clearly in error and the Circuit Court properly corrected this error.

After examining the language of the instruments and concluding that the petitioner was only an assignee, the Circuit Court considered the facts urged by petitioner in support of its direct obligee claim. In so doing,[26] the Circuit Court was merely showing that the facts were consistent with and supported, the legal conclusion. The Court was clearly within the province of appellate review.[27]

The following are the facts. The principal on this bond entered into a contract with Equitable by which he

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[26] Petitioner's Brief, p. 16.

[27] *Shafer v. Senseman,* 125 Pa. 310, 17 Atl. 350 (1889).

agreed to construct buildings on certain real estate and to assign to Equitable first mortgages on the real estate; Equitable on its part agreed to purchase these mortgages and to advance the purchase price as the work progressed in order to provide funds for the building operations. Before the delivery of the bond to the obligees, the principal and respondent executed the consent to assignment. The bond, the assignment and the consent to assignment were delivered under one backer to Equitable and Equitable Securities Corporation. Later the same day Equitable delivered them to petitioner along with the mortgages pledged by Equitable for a loan, the proceeds of which Equitable was free to use for any purposes Equitable saw fit.

Certainly there is nothing in these facts which is inconsistent with the plain language of the instruments. The language of the instruments is the primary source for determining the meaning. The surrounding facts, when consistent with that meaning, cannot be used as a basis for overthrowing it.

The petitioner has listed five facts which it contends support the so-called "finding" of the District Court.[28] The first is that respondent knew that petitioner was to be the ultimate recipient of the bond. The record discloses that respondent knew the bond was going to be *assigned* to petitioner. However, there is not one scintilla of evidence that petitioner expected to receive the bond in any other capacity than as an assignee.[29]

The second is that the assignment and consent to assignment were executed prior to delivery of the bond to the obligees. The signing of a simple consent to assignment prior to delivery of the bond is clearly without any legal significance to change the meaning of the language

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[28] Petitioner's Brief, p. 12.

[29] In some instances petitioner deliberately accepted *direct* obligations, and in others it accepted *assigned* obligations in precisely the same form as in the cases at bar. Appendix 150a et seq.

of the writings.[30] The bond and assignment, with the consent to assignment, were delivered by the respondent to Equitable,—not to the petitioner—and it was not until Equitable thereafter delivered them to the petitioner that the petitioner acquired rights under them.

The third fact is that the bond, assignment and consent to assignment were under one backer. What more natural and convenient way is there to keep together an assignment and the instrument assigned?

The fourth fact is that Equitable delivered the instruments to the petitioner the same day it received them. No act of Equitable with its assignee could be determinative of the rights and duties of the respondent under the bond.

The fifth fact is that the petitioner required the completion bond as collateral before it would loan its money to Equitable. The answer to this is that it received what it asked for. The bond assigned was sound protection against any default by the builder-principal. The effect of the District Court's holding that the petitioner was a direct obligee of the bond was to distort an ordinary surety completion bond into a bond which also insures an assignee against a default of its assignor-obligee, a result not justified by the plain language of the instrument.[31]

None of these five facts nor any other facts surrounding the execution and delivery of the bond, assignment and consent to assignment suggest that the parties intended those instruments to mean something contrary to their unambiguous terms. The District Court's conclusion that petitioner and not Equitable was the obligee of the bond was an erroneous conclusion of law; first, because it ignored the plain meaning of the language of those instruments contrary to the applicable rules of construction, and second, because the undisputed facts relied upon do not support

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[30] *Northwestern National Bank v. Commonwealth*, 345 Pa. 192, 27 A. (2d) 278 (1942). See Opinion of Circuit Court, Footnote 10. Petitioner's Brief, p. 19a.

[31] Appendix 15a et seq.

that conclusion. Even if the District Court's conclusion had been a finding of fact, it is clear from the foregoing discussion that such a finding would have been clearly erroneous under the judicial decisions applying Rule 52 (a). The Circuit Court of Appeals was therefore correct in reversing that conclusion and was clearly within the scope of appellate review in so doing.

The Circuit Court held that the petitioner was an assignee and applied the law of Pennsylvania that the rights of an assignee rise no higher than those of its assignor. Equitable, the assignor, having defaulted its obligation to the builder, thereby excused the builder from his obligation to perform the underlying contract and under the bond in suit. The assignor having no rights, the assignee has none.

II. The Circuit Court Properly Applied the Law of Pennsylvania in Holding That in the Absence of Default by a Principal Neither He Nor His Surety Are Liable on the Bond.

Petitioner, an assignee, seeks a construction of this bond the effect of which would be to permit an obligee to commit a breach of its contract with the builder so as to prevent the builder's completion of that contract,[32] and *despite that breach,* still recover from the surety and necessarily from the builder on the completion bond because the buildings were not built. To permit the Court to reach this conclusion petitioner argues that the bond obligation must be determined from the condition alone. This startling doctrine is not the law of Pennsylvania.

The rule of construction correctly applied by the Circuit Court in the cases at bar was the general rule that a

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[32] That the default by Equitable was the operative cause of non-completion of the houses by the principal is conceded. See Opinion of District Court, Petitioner's Brief, p. 3a.

bond must be interpreted in the light of the entire instrument, *inclusive of its recitals,* rather than from the condition alone.[33] This is the law of Pennsylvania. There are no exceptions.[34] The cases cited by petitioner are examples of, not exceptions to, that rule.

In *Young v. American Bonding Company,*[35] the plaintiff argued that the Court could not refer to the underlying contract in determining the obligation of the bond. The Court rejected that argument and held that the bond, the recitals of which are strikingly similar to those in the cases at bar, recited quite enough to "show that the engagement under the bond . . . was entered into on the common understanding that the mutual obligations of the parties thereunder would be faithfully observed." Contrary to the argument of petitioner[36] the Court gave no consideration whatever to the fact that the contract was referred to in the *condition.*

In *Phoenix Mill Company v. Kresge,*[37] the bond recited a sales agency contract covering the New York State area and was conditioned on the forwarding by the agent, within forty-five days, of all money due to the employer. The action was brought for money received by the agent from sales in Pennsylvania. The Court again refused to follow the contention that the obligation should be determined from the condition without regard to the recitals and held that, as the recitals referred to a New York sales agency, the bond obligation was limited to sales in that territory even though no such limitation was stated in the condition. The Court emphasized that to construe the bond otherwise was to make the recitals surplusage and meaningless.

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[33] *Phoenix Mill Company v. Kresge,* 254 Pa. 36, 98 Atl. 772 (1916); *Young v. American Bonding Company,* 228 Pa. 373, 77 Atl. 623 (1910).

[34] Petitioner's Brief, p. 21.

[35] Note 33, *supra.*

[36] Petitioner's Brief, p. 22.

[37] Note 33, *supra.*

That reasoning is equally applicable here. The second recital [38] expressly sets forth that Equitable was to advance moneys. Petitioner's contention that the obligation of the bond must be determined from the condition alone makes surplusage of this recital, which refers to a matter of vital concern to the surety's risk.

The *Phoenix* case, supra, was cited approvingly *and applied in favor of* a compensated corporate surety in *New Holland Dairies, Inc. v. Regent Dairy Products Corp.*,[39] where also the underlying contract of the parties was referred to in the *recitals*.

The above cases show the incorrectness of petitioner's assertion [40] that "In Pennsylvania the Courts look to the recitals of a bond to explain the condition thereof only in certain types of cases."

The cases cited by petitioner do not support that assertion. In *United States v. Morrisdale Coal Co.*,[41] the District Court did not even suggest that the condition was so indefinite as to be unenforceable. It conceded that the obligee's construction was tenable if the condition was to be read "literally and in vacuo" but held that a bond must be interpreted in the light of the recitals. In *Nazareth F & M Co. v. Marshall Co.*,[42] the problem considered by the court was whether the obligation should be construed in the light of the *entire* underlying contract referred to in the recitals, or only in the light of the *parts* thereof which had been set out in detail. Because parts had been set out in detail in the recitals, the court held that the bond obliga-

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[38] "Whereas, the Equitable Bonded Mortgage Company has agreed to advance One Hundred Forty-two Thousand Dollars ($142,000.) for the purchase of, and to be secured by assignments of first mortgages on the above mentioned dwellings, . . ." Appendix p. 16a.

[39] 115 Pa. Super. 87, 174 Atl. 664 (1934).

[40] Petitioner's Brief, p. 21.

[41] 50 F. Supp. 138 (D. C., E. D. Pa., 1942).

[42] 258 Pa. 558, 102 Atl. 268 (1917).

tion should be limited by those provisions and not the entire underlying contract.[43]

Petitioner further contends that *Dunbar v. Fleisher*[44] and the *Young* case, supra, were so decided *because* reference to the underlying obligation of the parties appeared in the condition of the bond. In neither opinion did the Court place any emphasis on whether the reference to the underlying obligation was in the condition or in the recitals. The decisions of the Pennsylvania appellate courts in the *Phoenix Mill*, the *New Holland Dairies*, and the *Nazareth* cases, all *supra*, and of the District Court in the *Morrisdale Coal Co.* case, *supra*—all cases where the reference to the underlying obligations appear in the recitals and not in the condition—disprove the existence of the rule asserted by petitioner.

Purdy v. Massey[45] is incorrectly stated by Petitioner as to both facts and law.

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[43] It is significant that the court indicated that had it not been for the details in the recitals it might have enforced the bond in the light of *all* the provisions of the contract referred to in the bond. 258 Pa at 564, 102 Atl. at 270.

[44] 137 Pa. 85, 20 Atl. 520 (1890).

[45] 306 Pa. 288, 159 Atl. 545 (1932). In that case, Massey, through an agent, entered into an agreement to purchase Mrs. Purdy's land for $85,000, of which $25,000 was to be paid in cash and the balance by a $60,000 purchase money first mortgage. The agreement further provided that if the purchaser determined to build a garage on the land in accordance with certain plans, Mrs. Purdy, upon being given a completion bond, would subordinate the $60,000 mortgage to the lien of a construction mortgage or mortgages in favor of others, in an amount not exceeding $80,000. Massey then executed a construction contract, in which it was provided that the construction mortgage funds would be retained by a mortgage agency and disbursed as work progressed. Mrs. Purdy accepted the $60,000 *second* mortgage, in lieu of her agreed first mortgage, upon the receipt of the completion bond in suit, which recited not only the building agreement but also the agreement of Mrs. Purdy to take the $60,000 second mortgage. The *use* of the

Petitioner's presentation of this case gives the impression that failure of consideration was a principal defense and that the case turned on that defense. Nothing could be less accurate.[46] The principal defense was impossibility of performance because of the injunction. This defense was rejected because the injunction was against the contemplated use, and not against construction. That this was the only defense considered by the Court is evident from its own statement:[47]

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proposed building as a public garage was enjoined as being in violation of zoning restrictions and Massey abandoned construction. The first mortgagee, having advanced the construction mortgage loan of $80,000, foreclosed, wiping out Mrs. Purdy's second mortgage, and she then instituted suit against Massey and his surety on the bond. The trial court's refusal to charge "there was no default on the part of the builder since the builder had never received the money payments required by the contract" (see Petitioner's Brief, p. 24) was fully justified by the "original record" to which Petitioner has referred.

[46] Petitioner makes the further error of assuming that it stands in the position of Mrs. Purdy as the direct obligee and that the principals stand in the position of Mr. Massey. This is not so. *Equitable* stands in the position of Mrs. Purdy, and the principals, the builders, stand in the position of Massey, with these very vital differences:

(1) Mrs. Purdy, the obligee, performed her part of the underlying agreement with Massey to take the second mortgage *which is referred to in the recital of the bond;* whereas, in the cases at bar, it is *stipulated* neither of the obligees performed their undertakings with the principals. (Stipulations 16 and 18, Appendix pp. 54a, 55a.)

(2) Massey, the builder, defaulted after Mrs. Purdy had performed, whereas in the cases at bar it is *stipulated* that the builders had not repudiated their obligation to build or abandoned construction or done anything in the nature of an anticipatory breach. (Stipulation 17, Appendix p. 54a.)

[47] 306 Pa. at 295, 159 Atl. at 547.

"Defendants contend that the injunction issued against (the builders) was a sufficient legal excuse and justification for their failure to erect the building. It is their only excuse, and it is neither legal nor sufficient."

The principal question with which both the Court and counsel were concerned was the measure of damages which depended upon whether the bond was one of guarantee or indemnity. The use by the Court of the term "absolute" relates only to the difference between a condition expressing indemnity and a condition expressing guaranty. The term bears no relationship to defenses against enforceability arising from the failure of an obligee to comply with its basic covenants as in the cases at bar. The Supreme Court of Pennsylvania held the surety as a guarantor of the performance by the principal, and nothing more. The analysis of this case by the Circuit Court, in the instant cases,[48] is incontrovertibly correct.

The Circuit Court here construed the bonds in the light of the recitals as is required by the decisions in Pennsylvania, and concluded that respondent's obligation was conditioned on a default by the principal on the underlying contract. Since it is expressly stipulated in the cases at bar that the principal was *not* in default, it held that respondent was not liable. The Circuit Court has reaffirmed the basic principles of law that the obligations of a surety are no greater than those of its principal,[49] and if the principal is not in default or if the obligee has failed to perform its obligations to the principal,[50] neither the obligee nor his assignee may claim against the principal or the surety on his bond. This is, and always has been, the

[48] Opinion of the Circuit Court, Petitioner's Brief, p. 21a.

[49] *McShain v. Indemnity Insurance Company of North America*, 338 Pa. 113, 12 A. (2d) 59 (1940).

[50] Restatement, Security (1941) § 126; Williston, Contracts (1936) § 1243; Restatement, Contracts (1932) §§ 274 (1), 279.

law of Pennsylvania. The Circuit Court did not err in either its interpretation or application of this law.

III. The Circuit Court Did Not Violate the Rule That Contracts of Paid Sureties Are to Be Construed Strictly Against Them.

The general rule stated by petitioner stands unchallegend, but it is inapplicable here. That rule is a secondary rule of construction which operates only when an uncertainty exists after consideration of the language of the instrument. No uncertainties exist in this case. The rule does not authorize a distortion of the language of an unambiguous instrument for the purpose of imposing liability on a paid surety where none otherwise exists.

> "The fact that the defendant was a paid surety and that the contract is, therefore, to be construed most strictly against it does not warrant a construction of words contrary to their clear intent."
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> *New Holland Dairies, Inc. v. Regent Dairy Products Corp.*, 115 Pa. Super. 87, at 91, 174 Atl. 664 (1934).
>
> Accord: *Commonwealth v. Cohen*, 140 Pa. Super. 361, 14 A. (2d) 362 (1940).
>
> *In Re Podolsky*, 115 F. (2d) 965, (C. C. A. 3, 1940).

It is worth noting that the documents here sued upon are identical in form and operative language with other bonds and assignments accepted and received by petitioner from Equitable in many prior transactions relating to other principals and other sureties.[51] Respondent, not petitioner, was the newcomer to these transactions. That petitioner was well aware of the nature of the obligations here accepted by it is evident from its deliberate acceptance in other cases of bonds which ran directly in its favor as

[51] Testimony of Mr. Scattergood, Appendix 137a, 139a, 150a.

obligee and which made no reference in the recitals to the underlying contract between the builders and Equitable.[52]

IV. The Circuit Court of Appeals Did Not Apply Inconsistent Standards of Construction in Reaching Its Decision.

Petitioner urges that the Circuit Court applied "a rule of strict construction to the benefit of the paid surety" in concluding that petitioner's rights under the bond were those of an assignee. The Circuit Court examined the plain and unambiguous meaning of the language of the instruments, considered the undisputed facts, and followed that plain and unambiguous meaning. This is neither a strict nor a liberal interpretation. It is the *only* interpretation which can be reached without completely and unjustifiably distorting the language of those instruments.

Petitioner urges further that the Circuit Court adopted "a liberal and strained construction"[53] in concluding that the condition of the bond excused the obligors when the obligee had breached his contract and caused the failure complained of. In so doing it adopted the only reasonable construction possible and the construction it was required to adopt under the Pennsylvania decisions.

* * *

It is respectfully submitted that no one of the reasons advanced by the petitioner in support of its Petition is sound and that there is no occasion for review by this Court of the decision of the Circuit Court of Appeals.

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March 1, 1946.

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[52] Testimony of Mr. Scattergood, Appendix 152a, 154a; Defendant's Exhibits 21 and 22; Appendix 250a, 253a.

[53] Petitioner's Brief, p. 32.